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No. 10610

United States
Circuit Court of Appeals
For the Ninth Circuit.

JAMES GOODWIN POWELL and ANNA STRACHAN POWELL, husband and wife,
Appellants,

vs.

PETER J. WUMKES,
Appellee.

Transcript of Record

Upon Appeal from the District Court of the United States for the Southern District of California, Central Division

Rotary Colorprint, 590 Folsom St., San Francisco

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NAMES AND ADDRESSES OF ATTORNEYS:

For Appellants:

H. R. GRIFFIN

408-10 Katz Bldg.
San Bernardino, Calif.

For Appellee:

NICHOLS, COOPER and HICKSON and
C. P. VON HERZEN

412-18 First National Bldg.
Pomona, Calif. [1*]

*Page numbering appearing at foot of page of original certified Transcript of Record.

United States District Court, Southern District of California, Central Division.

No. 36775-C

In the Matter of

JAMES GOODWIN POWELL and ANNA STRACHAN POWELL,

Bankrupts

PETITION BY DEBTOR WITH SCHEDULES A AND B

DEBTOR'S PETITION

In Proceedings Under Section 75 of the Bankruptcy Act

To the Honorable.....
Judge of United States District Court
for the Southern District of California

The Petition of James Goodwin Powell and Anna Strachan Powell, husband and wife, of 905 West Lugonia Ave. Redlands, in the County of San Bernardino and District and State of California

Trade, or Business of
Occupation, Citrus Growers

Respectfully Represents:
That they are personally bonifide engaged primarily in farming operations (or that the principal part of their income is derived from farming operations) as follows: The growing of citrus products.
That said debtors further allege that all property

scheduled herein is jointly owned, and all debts scheduled herein are jointly owed, by said debtors, James Goodwin Powell and Anna Strachan Powell. That such farming operations occur in the county (or counties) of San Bernardino, within said judicial district; that they are insolvent (or unable to meet their debts as they mature); and that they desire to affect a composition or extension of time to pay their debts under section 75 of the Bankruptcy Act.

That the schedule hereto annexed, marked "A," and verified by your petitioner's oath, contains a full and true statement of all his debts, and (so far as it is possible to ascertain) the names and places of residence of their creditors, and such further statements concerning said debts as are required by the provisions of said act.

That the schedule hereto annexed, marked "B," and verified by your petitioner's oath, contains an accurate inventory of all their property, both real and personal, and such further statements concerning said property as are required by the provisions of said act.

Wherefore Your Petitioner Prays, That the petition may be approved by the Court and proceedings had in accordance with the provisions of said section.

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioners

H. R. GRIFFIN
Attorney for Petitioner
408 Katz Bldg., San Bernardino, California.

United States of America
Southern District of California—ss.

I, James Goodwin Powell and Anna Strachan Powell the Petitioning debtor mentioned and described in the foregoing petition, do hereby make solemn oath that the statements contained therein are true according to the best of my knowledge, information and belief.

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

Subscribed and sworn to before me, this 20th day of July, A. D. 1940

[Seal] H. R. GRIFFIN
Notary Public [2]

SUMMARY OF DEBTS AND ASSETS

Form

(From the Statements of the Bankrupt in Schedules A and B)

Schedule A....	1	(1)	Taxes and Debts due United States	
" A....	1	(2)	Taxes due States, Counties, Districts and Municipalities	250.00
" A....	1	(3)	Wages	
" A....	1	(4)	Other debts preferred by law.....	
" A....	2		Secured claims	22,270.15
" A....	3		Unsecured claims	
" A....	4		Notes and bills which ought to be paid by other parties thereto	
" A....	5		Accommodation paper	
			Schedule A, total.....	22,520.15
Schedule B....	1		Real Estate	14,000.00
" B....	2-a		Cash on hand	
" B....	2-b		Bills, promissory notes and securities	
" B....	2-c		Stock in trade	
" B....	2-d		Household goods, etc.	500.00
" B....	2-e		Books, prints and pictures.....	50.00
" B....	2-f		Horses, cows and other animals..	
" B....	2-g		Carriages and other vehicles.....	450.00
" B....	2-h		Farming stock and implements..	65.00
" B....	2-i		Shipping and shares in vessels....	
" B....	2-k		Machinery, tools, etc.	
" B....	2-l		Patents, copyrights and trade marks	
" B....	2-m		Other personal property	
" B....	3-a		Debts due on open account.....	
" B....	3-b		Stocks, negotiable bonds, etc.....	
" B....	3-c		Policies of insurance	3,000.00
" B....	3-d		Unliquidated claims	
" B....	3-e		Deposits of money in banks and elsewhere	

Schedule A (2)—(Continued)

	Dollars Cents
1 1938 Ford Sedan with an encumbrance thereon in favor of the Bank of America in the sum of $450.00	450.00
Total	22,270.15

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL

Petitioner

(3) [5]

SCHEDULE A (3)

Creditors Whose Claims Are Unsecured

(N. B.—When the name and residence (or either) of any drawer, maker, endorser or holder of any bill or note, etc., are unknown, the fact must be stated, also the name and residence of the last holder known to the debtor. The debt due to each creditor must be stated in full, and any claim by way of set-off stated in the schedule of property).

Reference to Ledger or Voucher—Names of Creditors—Residence (if unknown, that fact to be stated.) Where and when contracted—Nature and consideration of the debt, and whether any judgment, bond, bill of exchange, promissory note, etc., and whether contracted as partner or joint contractor with any other person, and if so with whom.	Dollars Cents
	None

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL

Petitioner

(4) [6]

SCHEDULE A (4)

Liabilities on Notes or Bills Discounted Which Ought to be Paid by the Drawers, Makers, Acceptors or Indorsers

(N. B.—The dates of the notes or bills, and when due, with the names, residences, and the business or occupation of the drawers, makers or acceptors thereof, are to be set forth under the names of the holders. If the names of the holders are not known, the name of the last holder known to the debtor shall be stated, and his business and place of residence. The same particulars as to notes or bills, on which the debtor is liable as indorser.)

	Dollars Cents
Place where contracted—Whether liability was contracted as partner or joint contractor or with any other person; and if so, with whom. Reference to Ledger or Voucher—Names of holders so far as known—Residence (if known, that fact must be stated).	
	None

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

(5) [7]

SCHEDULE A (5)

Accommodation Paper

(N. B.—The dates of notes or bills, and when due, with the names and residences of the drawers, makers and acceptors thereof, are to be set forth under the names of the holders; if the bankrupt be liable as a drawer, maker, acceptor or indorser thereof, it is to be stated accordingly. If the names of the holders are not known, the name of the last holder known to the debtor should be stated, with his residence. Same particulars as to the other commercial paper).

	Dollars Cents
Reference to Ledger or Voucher—Names of Creditors—Residence (if unknown, that fact to be stated). Where and when contracted—bill of exchange, promissory note, etc., and whether contracted as partner. Nature and consideration of the debt, and whether any judgment, bond, or joint contractor with any other person, and if so with whom.	
	None

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

Schedule B (1)—(Continued)

	Dollars Cents
quarter of Section 21, Township 1 South, Range 3 West, San Bernardino Base & Meridian, in the City of Redlands, County of San Bernardino, State of California, according to Government Survey described as follows: Beginning at a point on the east boundary line of the above described tract, which is 718.07 feet north from the southeast corner thereof; thence running north along the east boundary line thereof 597.08 feet, more or less, to the northeast corner of said tract; thence west along the north boundary line thereof, 311.13 feet, more or less, to a point which is 1,008.87 feet east from the northwest corner of said tract; thence southerly on a line parallel with the east boundary of said tract 597.08 feet, more or less, to a point due west of the point of beginning; thence east 311.13 feet, more or less, to the beginning. Together with 5 shares of the capital stock of the Lugonia Water Company, a corporation	6,000.00
Total.....	14,000.00

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

(7) [9]

SCHEDULE B (2)

Personal Property

Dollars Cents

A. Cash on Hand
None

B. Bills of Exchange, promissory notes, or securities of any description, (each to be set out separately).
None

C. Stock in trade in business of at of the value of
None

Schedule B (2)—(Continued)

	Dollars Cents
D. Household goods and furniture, household stores, wearing apparel and ornaments of the person, viz:	
	$500.00
Total.....	$500.00

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

(8) [10]

SCHEDULE B (2)—(Continued)

Personal Property

E. Books, prints and pictures, viz:	50.00
F. Horses, cows, sheep and other animals (with number of each), viz:	None
G. Carriages and other vehicles, viz:	
1 1938 Ford Sedan	450.00
H. Farming stock and implements of husbandry, viz:	
1 old Truck—$25.00	
1 old Tractor—$35.00	
1 Disc—$5.00	65.00
Total.....	565.00

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

(9) [11]

SCHEDULE B (2)—(Continued)

Personal Property

I. Shipping and shares in vessels, viz:	None

Schedule B (2)—(Continued)

Dollars Cents

K. Machinery, fixtures, apparatus and tools used in business, with the place where each is situated, viz:

Miscellaneous hoes, spades, rakes, etc., being hand tools.

L. Patents, copyrights and trademarks, viz:

None

M. Goods or personal property of any other description, with the place where each is situated, viz:

None

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

SCHEDULE B (3)

Choses in Action

A. Debts due petitioner on open account — None

B. Stock in incorporated companies, interest in joint stock companies, and negotiable bonds. — None

C. Policies of Insurance.

Life Insurance Policy — $3,000.00

D. Unliquidated Claims of every nature with their estimated value.

A certain number of revolving certificates in the Redlands Heights Groves, Inc. packing house, the exact amount being undetermined.

The proceeds from certain crops already picked by said Redlands Heights Groves, Inc. packing house, the same being undetermined.

E. Deposits of money in banking institutions and elsewhere. — None

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

SCHEDULE B (4)

Property in Reversion, Remainder or Expectancy, Including Property Held in Trust for the Debtor or Subject to Any Power or Right to Dispose of or to Charge.

N. B.—A particular description of each interest must be entered. If all, or any of the debtor's property has been conveyed by deed of assignment or otherwise, for the benefit of creditors, the date of such deeds should be stated, then name and address of the person to whom the property was conveyed; the amount realized from the proceeds thereof, and the disposal of the same, as far as known to the debtor.

General Interest	Particular Description	Supposed Value of My Interest Dollars Cents
Interest in land.		
None		
Personal property.		
None		
Property in money, stocks, shares, bonds, annuities, etc.		
None		
Rights and powers, legacies and bequests.		
None	Total.....	

Amount realized from Proceeds of Property Conveyed

Property heretofore conveyed for the benefit of Creditors.

What portion of Debtor's property has been conveyed by deed of assignment, or otherwise for benefit of creditors; date of such deed, name and address of party to whom conveyed; amount realized therefrom, and disposal of same, so far as known to debtor.

None

What sum or sums have been paid to counsel, and to whom for services rendered or to be rendered in this bankruptcy.

None

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

SCHEDULE B (5)

A particular statement of the Property claimed as Exempt from the Acts of Congress relating to Bankruptcy, giving each item of Property and its valuation; and if any portion of it is Real Estate, its location, description and present use.

Dollars Cents

Military uniforms, arms and equipments.

None

Property claimed to be exempt by State Laws; its valuation; whether real or personal; its description and present use; and reference given to the statute of the State creating the exemption.

Household Furniture $500.00

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

(13) [15]

SCHEDULE B (6)

Books, Papers, Deeds and Writings Relating to Bankrupt's Business and Estate

The following is a true list of all books, papers, deeds and writings relating to my trade, business dealings, estate and effects, or any part thereof, which at the date of this petition, are in my possession, or under my custody or control, or which are in the possession or custody of any peron in trust for me, or for my use, benefit or advantage; and also of all others which have been heretofore, at any time, in my possession or under my custody or control, and which are now held by the parties whose names are hereinafter set forth, with the reason for their custody of the same.

Dollars Cents

Books	None
Deeds	None
Papers	None

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioner

OATH TO SCHEDULE B

United States of America
Southern District of California
Central Division—ss.

On this 20th day of July, A. D. 19 , before me, personally came James Goodwin Powell and Anna Strachan Powell the person mentioned in and who subscribed to the foregoing schedule and who, being by me first duly sworn, did declare the said schedule to be a statement of all their estate, both real and personal, in accordance with the Acts of Congress relating to bankruptcy.

[Seal] H. R. GRIFFIN
(Notary Public)

(14)

[Endorsed]: Filed July 25, 1940. [16]

[Title of District Court and Cause.]

APPROVAL OF DEBTOR'S PETITION AND ORDER OF REFERENCE

(under Section 75 Bankruptcy Act)

At Los Angeles, in said District, on July 25, 1940, before the said Court the petition of James Goodwin Powell and Anna Strachan Powell, husband and wife, that they desire to effect a composition or an extension of time to pay their debts, and such other relief as may be allowed under the Act of March 3, 1933, and within the true intent and meaning of all the Acts of Congress relating to bankruptcy, having been heard and duly considered, the said petition is hereby approved accordingly.

It is thereupon ordered that said matter be referred to Fred Duffy, Esq., one of the Conciliation Commissioners in bankruptcy of this Court, to take such further proceedings therein as are required by said Acts; and that the said James Goodwin Powell and Anna Strachan Powell, husband and wife, shall attend before said Conciliation Commissioner on August 1, 1940, and at such time said Conciliation Commissioner shall designate, at his office in San Bernardino California, and shall submit to such orders as may be made by said Conciliation Commissioner or by this Court relating to said matter.

Witness, the Honorable Paul J. McCormick, Judge of said Court, and the seal thereof, at Los Angeles, in said District, on July 25, 1940.

R. S. ZIMMERMAN,
Clerk
By F. BETZ
Deputy Clerk

[Endorsed]: Filed July 25, 1940. [18]

[Title of District Court and Cause.]

AMENDED PETITION

To the Honorable Paul J. McCormick Judge of the District Court of the United States, for the District above set forth:

Your petitioners, the above named James Goodwin Powell and Anna Strachan Powell, would

show unto your Honor, that they did on the 20th day of July, 1940 file in this Court, a petition under Section 75 of the Bankruptcy Act, as amended, which petition is still pending, that they have been unable to obtain acceptance of the majority in number and amount of all creditors, whose claims are affected by the composition and extension proposal, which they submitted at the First Meeting of Creditors, to the Conciliation Commissioner, appointed by this Court.

That as permitted by the first paragraph of Sub Section (s) Section 75 of the Bankruptcy Act, as amended, they do hereby amend their petition heretofore filed on the 20th day of July, 1940 and they do substitute for the provisions of said petition as may be in conflict with this amendment, the contents of this amendment.

And They Pray that they may be adjudged Bankrupt, that proceedings may be had in regard to any and all property in conformity with the law in regard to procedure under Sub Section (s) of Section 75 of the Bankruptcy Act, as amended.

That all their property wherever located, whether pledged, encumbered or unencumbered, be appraised; that the unencumbered exemptions and unencumbered interest or equity in their exemptions as prescribed by the law of the State of California, [19] as set forth in the schedules heretofore filed in this matter, be set aside and set off to them; and that they be allowed to retain possession under the supervision and control of the Court, of any part or parcel or all of the remainder of property includ-

ing their enuncumbered exemptions and pay for the same under the terms and conditions of Sub Section (s) of Section 75 of the Bankruptcy Act, as Amended.

He Further Pray for all needful and lawful proceedings under the provisions of law which do become applicable on the filing of this petition and particularly those provisions contained in Sub Section (s) of Section 75 of the Bankruptcy Act, as Amended.

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL
Petitioners

United States of America,
Southern District of California,—ss.
County of San Bernardino

James Goodwin Powell and Anna Strachan Powell, the petitioning debtors mentioned and described in the foregoing amended petition, do hereby make solemn oath that the statements contained herein are true to the best of my knowledge, information and belief.

JAMES GOODWIN POWELL
ANNA STRACHAN POWELL

Subscribed and sworn to before me this 17th day of October, 1940.

[Seal] H. R. GRIFFIN
Notary Public in and for said County and State.

[Endorsed]: Filed Oct. 24, 1940. [20]

[Title of District Court and Cause.]

CERTIFICATE OF CONCILIATION COMMISSIONER

I, Fred Duffy, the Conciliation Commissioner of the above entitled Court, in and for the County of San Bernardino, do hereby certify that the Composition and/or Extension has failed, and I hereby make the following recommendation to the Honorable Judge of the above entitled Court, to-wit:

That James Goodwin Powell and Anna Strachan Powell be adjudicated bankrupt under and pursuant to Section 75 (s) of the Bankruptcy Act.

Dated: October 23rd, 1940.

FRED DUFFY
Conciliation Commissioner for San Bernardino County, California.

[Endorsed]: Filed Oct. 24, 1940 [22]

[Title of District Court and Cause.]

ADJUDICATION, ORDER OF REFERENCE, AND TEMPORARY RESTRAINING ORDER

Under Section 75-s, Bankruptcy Act.

At Los Angeles, in said District, on October 24, 1940 before said Court in Bankruptcy, the Petition of James Goodwin Powell and Anna Strachan Powell, husband and wife debtors in the above-

termine value of real property of above named debtors.

That on the 22nd., day of April, 1943, Hearing of said petition was set by this commissioner, for the 18th day of May, 1943. Notice of said hearing was given by mail to all parties in interest.

That on the 18th day of May, 1943, said petition came on for hearing. Present at said hearing were debtors and their attorney, the Honorable H. R. Griffin, petitioning creditor Peter J. Wumkes, was not personally present, but was represented by his attorneys, Nichols, Cooper & Hickson, by Donald P. Nichols.

That on the 18th day of May, 1943, the petition or motion was denied.

That on the 1st., day of June, 1943, Order was entered by this commissioner, extending time for filing petition for review of order dated May, 18th., 1943, to the 1st. day of July, 1943. [25]

On the 3rd., day of June, 1943, Order was entered extending time for filing petition for review of commissioner's order, dated May, 18th., 1943, to June, 15th., 1943.

That on the 11th day of June, 1943, Creditor, Peter J. Wumkes, filed petition to review order of the Conciliation Commissioner, dated May, 18th., 1943.

SUMMARY OF EVIDENCE

No evidence to sustain allegations of petition for rehearing to determine value of real property was introduced on behalf of petitioner, Peter J. Wumkes. The matter resolved itself into a case of At-

torney for debtors arguing against granting of petition and Attorney for petitioning creditor, argued in favor of granting said petition.

Russell Goodwin, former attorney for petitioning creditor was present and testified that the last address and only address of Peter J. Wumkes, that he knew of was 922 East Lugonia Ave., Redlands, California. That Peter J. Wumkes, at one time furnished him, said Goodwin, a telephone number, Arizona 9-3551 Los Angeles, to call him at, that said Goodwin called said number on February, 13th., 1943, and was informed by telephone operator, no such number and no name listed thereunder. Said Russell Goodwin, exhibited to and left with this commissioner, two envelopes, one bearing postmark dated February, 12, 1943, and one bearing postmark, dated February 13th, 1943, which envelopes contained certain contents which were removed by said Goodwin, and the envelopes deposited with this commissioner, which said envelopes are hereto attached and made a part of this certificate.

QUESTION PRESENTED

The question presented by the petition for review is: Did the Conciliation Commissioner-Referee, err in denying petition or motion for rehearing to determine value of real [26] property of debtors.

PAPERS SUBMITTED

1. Petition for Rehearing to Determine Value of Real Property.

2. Notice of Hearing said Petition or Motion.

3. Order Denying said Petition or Motion for Rehearing.

4. Notice of entry of Order Denying Petition for Rehearing to determine value of Real Property.

5. Order extending time to file Petition for Review of Order, Dated May, 18th., 1943.

6. Order extending time to file Petition for Review.

7. Petition for Review.

8. Two envelopes deposited with Commissioner, by Russell Goodwin, addressed to Peter J. Wumkes, and returned to writer by United States Postoffice Department, with notation thereon. Dated July, 5th., 1943.

Respectfully submitted,
FRED DUFFY
Conciliation Commissioner-Referee [27]

[Title of District Court and Cause.]

PETITION TO REVIEW ORDER OF THE CONCILIATION COMMISSIONER UNDER DATE OF MAY 18, 1943

Comes now your petitioner, Peter J. Wumkes, and respectfully shows:

I.

Petitioner is a secured creditor of the above-named bankrupts, and filed his proof of secured

debt in these proceedings, which proof of debt was duly allowed. In this respect your petitioner specifically refers to the said proof of secured debt and incorporates it herein with the same force and effect as though set out in full.

II.

The above-captioned proceedings were instituted on the 25th day of July, 1940, and thereafter the proceedings were referred to Hon. Fred Duffy, United States Conciliation Commissioner for the County of San Bernardino. Thereafter and on or about the 25th day of October, 1940, the above-named bankrupts filed their amended petition and were duly adjudicated bankrupts under the provisions [28] of Sub-section (s) of Section 75 of the United States Bankruptcy Act. Thereafter, and on or about the 16th day of June, 1941, the said Conciliation Commissioner made and entered his order staying proceedings for a period of three years and setting as rental during such period one-quarter of the gross proceeds of all agricultural income produced on the agricultural real property of the above-named bankrupts, said rent to be paid annually commencing June 16, 1942. In this respect petitioner refers to and incorporates herein the said rent order and order staying proceedings with the same force and effect as though set out in full herein.

III.

Petitioner has not received any rent whatever pursuant to the order set out in Paragraph II

above from the Conciliation Commissioner nor from the bankrupts, or either of them, and in this respect petitioner is informed and believes and therefore alleges that the said rent order has not been honored with compliance and is now in default and has at all times mentioned herein been in default.

IV.

On or about the 23rd day of December, 1942, the above-named bankrupts filed a petition requesting a hearing to determine the value of the real property involved in the above-captioned proceedings, and thereafter, following several postponements, said petition came on for hearing before the said Conciliation Commissioner. At the time of the said hearing but prior to the introduction of any evidence therein, your petitioner's attorney requested the Conciliation Commissioner's permission to withdraw from the case and thereupon did withdraw from the case, leaving your petitioner unrepresented in the reappraisal proceedings which then followed. In this connection, petitioner had no prior knowledge whatever of his attorney's intention to withdraw, and by virtue of this fact was left unrepresented by counsel and totally unprepared [29] to present evidence regarding the value of the real property securing petitioner's claim or to rebut evidence introduced by the attorney for the bankrupts, and was without the legal skill and technical ability to cross-examine witnesses produced by the bankrupts through their counsel.

V.

Thereafter and on or about the 20th day of April, 1943, your petitioner filed with the said Conciliation Commissioner a petition for rehearing, which petition for rehearing was predicated on the facts and circumstances flowing from and surrounding the withdrawal of petitioner's attorney without notice to petitioner at a time when petitioner could not secure counsel for representation in the reappraisal proceedings.

VI.

Said petition for rehearing regularly came on for hearing May 18, 1943, and after hearing said petition the said Commissioner made and entered his order denying the petition for rehearing the bankrupts' petition to determine value of the real property concerned in these proceedings. Said order denying your petitioner's petition for rehearing was made and entered the day such petition was heard and is unsupported by findings or conclusions.

VII.

The order of May 18, 1943, denying your petitioner's petition for rehearing of the bankrupts' petition to determine value of the real property concerned in these proceedings is erroneous in the following particulars:

1. It was inequitable and improper for the Commissioner to deny petitioner a rehearing of the reappraisal proceedings where such denial would have the effect of preventing petitioner from ever presenting appropriate evidence regarding the value

of the real property underlying his secured claim through adequate counsel, and in this respect your petitioner urges that the [30] refusal of the Commissioner to grant a rehearing under the circumstances surrounding the original "hearing" is a deprivation of due process of law to your petitioner.

2. The said order of May 18, 1943, is unsupported by findings of fact or conclusions of law, particularly a finding of fact and a conclusion of law predicated thereupon to the effect that the rent order theretofore made and entered in these proceedings had been honored with compliance and was current.

Wherefore, Petitioner, feeling aggrieved by the provisions of said order of May 18, 1943, prays that it may be reviewed, as provided by the Bankruptcy Act and amended, modified or set aside in such respects as to the Court seems meet and equitable.

Respectfully submitted,

PETER J. WUMKES

Petitioner.

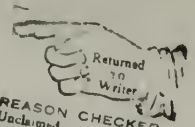
NICHOLS, COOPER & HICKSON,

By DONALD P. NICHOLS

Attorneys for Petitioner.

[Endorsed]: Filed 6/11/43. Fred J. Duffy, Council, Comm. [31]

RUSSELL GOODWIN
ATTORNEY AT LAW
SECURITY-FIRST NATIONAL BANK BUILDING
REDLANDS, CALIFORNIA



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Gone
RJ

Dr. Peter J. Wumkes
922 E. Lugonia Avenue
Redlands, California

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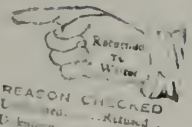
RUSSELL GOODWIN
ATTORNEY AT LAW
SECURITY-FIRST NATIONAL BANK BUILDING
REDLANDS, CALIFORNIA



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Dr. Peter J. Wumkes
922 E. Lugonia Avenue
Redlands, California

[Title of District Court and Cause.]

ORDER EXTENDING TIME FOR FILING PETITION FOR REVIEW

It Is Hereby Ordered that the time for filing a Petition for Review of the Order denying the petition of Peter J. Wumkes for a rehearing to determine value of real property made on the 18th day of May, 1943, be, and the same is hereby extended to June 15th, 1943.

Dated this 3rd day of June, 1943.

FRED DUFFY
Conciliation Commissioner for
San Bernardino County,
California [34]

[Title of District Court and Cause.]

ORDER EXTENDING TIME FOR FILING PETITION FOR REVIEW

It is Hereby Ordered that the time for filing a Petition for Review of the order denying the petition of Peter J. Wumkes for a rehearing to determine value of real property made on the 18th day of May, 1943, be, and the same is hereby extended to July 1st, 1943.

Dated this 1st day of June, 1943.

FRED DUFFY
Conciliation Commissioner for
San Bernardino County,
California

[Endorsed]: Filed 6/1/43. Fred Duffy, Council Comm. [35]

[Title of District Court and Cause.]

NOTICE OF ORDER DENYING PETITION FOR REHEARING TO DETERMINE VALUE OF REAL PROPERTY

To Peter J. Wumkes and his attorneys, Nichols, Cooper and Hixon, Esqs., and to all other creditors of James Goodwin Powell and Anna Strachan Powell, Redlands, San Bernardino County, and District and State aforesaid, Bankrupts:

Notice is hereby given that on the 18th day of May, 1943, the Honorable Fred Duffy, Conciliation Commissioner and Referee of the above-entitled Court, did duly and regularly after a hearing thereon, enter his order denying the Petition of Peter J. Wumkes for a rehearing to determine value of real property.

Dated this 18th day of May, 1943.

FRED DUFFY
Conciliation Commissioner and Referee.

[Endorsed]: Filed 5/18/43. Fred Duffy, Council Comm. [36]

[Title of District Court and Cause.]

ORDER DENYING PETITION FOR REHEARING TO DETERMINE VALUE OF REAL PROPERTY

The above-entitled matter coming on regularly before the Honorable Fred Duffy, Conciliation Com-

missioner, of the above-entitled Court in and for the County of San Bernardino, State of California, on the 18th day of May, 1943, at the hour of 10 o'clock A. M., upon a Petition filed by Peter J. Wumkes, requesting a rehearing to determine the value of real property, and it appearing to the Court that due and regular notice of said hearing has been given in accordance with the law, and the said Peter J. Wumkes appearing by his attorneys, Nichols, Cooper and Hixon, and the debtor, James Goodwin Powell, appearing in person and through his attorney, H. R. Griffin, who also appeared for Anna Strachan Powell, the other debtor, and no further appearances being made; and evidence, both oral and documentary, having been introduced and witnesses examined, and the cause having been argued by respective counsel, and the matter being duly and regularly submitted to the Court, and the Court being fully advised of the law and the facts in the premises

Now, Therefore, It Is Hereby Ordered:

That the Petition of Peter J. Wumkes for rehearing to determine value of real property is hereby denied.

Dated this 18th day of May, 1943.

FRED DUFFY
Conciliation Commissioner for
San Bernardino County,
California.

[Endorsed]: Filed 5/18/43, Fred Duffy, Council Comm. [37]

[Title of District Court and Cause.]

NOTICE OF HEARING

You and Each of You Will Please Take Notice that on the 18 day of May, 1943, at the hour of ten o'clock A. M., or as soon thereafter as counsel can be heard, at the office of Fred Duffy, Conciliation Commissioner for San Bernardino County, California, at #318 Katz Building, San Bernardino, Peter J. Wumkes, creditor of the above-named debtors will move the Court for an order of rehearing to determine value of real property of the above-named debtors upon which said creditor has a secured lien.

Said motion will be based upon the petition filed by the above-named creditor and the filings and records in the above-entitled matter.

Dated this 22 day of April, 1943.

FRED DUFFY
Conciliation Commissioner for
San Bernardino County,
California.

DPN:B

[Endorsed]: Rec'd and filed 4/20/43. Fred Duffy, Council Comm. [38]

[Title of District Court and Cause.]

PETITION FOR REHEARING TO DETERMINE VALUE OF REAL PROPERTY

Comes now Peter J. Wumkes and respectfully represents as follows:

I.

That on or about the 25th day of July, 1940, the above-named Debtors filed their joint petition in the above entitled Court praying for relief as provided for in Section 75 of the Bankruptcy Act.

II.

That on or about the 25th day of October, 1940, said Debtors having been unable to secure acceptance or confirmation of an extension proposal filed their amended petition and were adjudicated bankrupts in accordance with the provisions of Section 75-s of the Bankruptcy Act.

III.

That thereafter, on or about the 1st day of November, 1940, an appraisal was made of the properties of Debtors and the property upon which your petitioner was a secured lien holder was thereupon appraised by one, George W. Holbrook, for the sum of $5,200.00, which appraisal was, thereafter, on the 24th day of November, 1940, approved and confirmed by Honorable Fred Duffy, Conciliation Commissioner.

IV.

That on or about the 23rd day of December, 1942, the [39] said Debtors filed their joint petition requesting re-appraisal or hearing to determine value of their real property and that pursuant to said petition a meeting of creditors was called by the Honorable Fred Duffy, Conciliation Commissioner, to hear and determine the value of the Debtors'

real property, which hearing was set for the 2nd day of February, 1943, and thereafter continued for hearing, and the matter was finally heard on the 3rd day of March, 1943.

V.

That prior to the date set for the hearing of said petition to determine value of said property, your petitioner made several efforts to contact his attorney, Russell Goodwin, but was unable to do so and although your petitioner left his telephone number and address and requested that Goodwin contact him, your petitioner did not hear anything from his said attorney, Russell Goodwin, prior to the said date of March 3, 1943. That upon arrival at the said hearing, your petitioner's attorney requested to withdraw from the case. That your petitioner did not desire to retain counsel who did not wish to represent him and therefore consented to such withdrawal. That your petitioner believed that the said attorney, Russell Goodwin, had obtained witnesses for the purpose of assisting the Court in determining the true value of the property; that said attorney had done nothing in preparation for said hearing. That after he withdrew as counsel for your petitioner the hearing then proceeded, and while your petitioner was afforded the opportunity of cross-examining Debtors' witnesses, your petitioner felt he was without legal experience and did not know what questions could be asked of said witnesses. That your petitioner, through mistake and excusable neglect, was not afforded the

opportunity of subpoenaing witnesses on his behalf to attend said trial and to aid the Court in [40] determining the true value of said real property.

VI.

That on or about the 9th day of April, 1943, the Honorable Fred Duffy, Conciliation Commissioner, entered his order determining the value of the property upon which petitioner had his secured claim to be of the value of $3,900.00. That in truth and in fact said property is reasonably valued far in excess of said amount and to allow Debtors to redeem said property at said price or to allow said valuation to stand, would result in a gross injustice and inequity as far as your petitioner is concerned.

VII.

That the secured lien of your petitioner on said property is in excess of $14,000.00.

VIII.

That your petitioner believes, and therefore alleges, that he should be granted an opportunity to present testimony and produce evidence to show the true and correct value of said property, and requests that an order be made for a re-hearing of Debtors' petition for a determination of value of the property securing your petitioner's lien.

Wherefore, your petitioner prays that a time be set for the hearing of this petition and that thereafter the Court make its order allowing your

petitioner to present additional evidence and testimony regarding the value of said real property.

PETER J. WUMKES
Petitioner.

NICHOLS, COOPER & HICKSON,
Pomona, California.
Attorneys for Petitioner. [41]

State of California,
County of Los Angeles.—ss.

Peter J. Wumkes, being by me first duly sworn, deposes and says:— That he is the petitioner in the foregoing and above entitled action; that he has read the foregoing Petition for Rehearing to Determine Value of Real Property and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon his information or belief, and as to those matters that he believes it to be true.

PETER J. WUMKES

Subscribed and sworn to before me this 15th day of April, 1943.

[Seal] ALICE M. KESTERSEN
Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Rec'd and filed 4/20/43. Fred Duffy, Council Comm. [42]

[Endorsed]: Filed July 19, 1943. Edmund L. Smith, Clerk, by E. M. Enstron, Deputy.

[Title of District Court and Cause.]

CERTIFICATE ON REVIEW OF CONCILIATION COMMISSIONER'S ORDER OF APRIL, 9. 1943, FINDING VALUE OF REAL PROPERTY

I, Fred Duffy, Conciliation Commissioner of above entitled Court, for the county of San Bernardino, State of California, before whom above entitled matter is pending under proceedings pursuant to the provisions of Section 75 of the Bankruptcy Act.

Do Hereby Certify.

That above named debtors filed their petition in the of Extension Proposal by their creditors, did on the 25th day of July, 1940, that said petition was approved and the matter referred to Fred Duffy, Esq., Conciliation Commissioner, for further proceedings.

That debtors having failed to secure acceptance of Extension Proposal by their ceditors, did on the 24th day of October, 1940, file in said Clerk's office, their Amended Petition under sub Section (s) of Section 75 of the Bankruptcy Act.

Debtors were adjudicated and matter referred to said Fred Duffy, acting as Referee for further proceedings. That certain proceedings were had thereon and on the 23rd., day of December, 1942, said debtors filed in the office of said Commissioner, a Petition requesting reappraisal or Hearing to determine value of debtors Real Property.

That said Real Property consists of two portions,

One, 5.78 acres on which one, Peter J. Wumkes, holds encumbrance and the other consisting of 4.20 acres, on which one, Frank C. Clark, holds encumberance. That said two portions are joined and considered as one Orange Grove.

That the portion of said Real Property on Which Peter J. Wumkes, holds encumbrance, is unimproved except the Citrus Trees thereon. [43]

That on the 20th day of January, 1943, this Commissioner mailed to each creditor shown by the schedules on file herein, a Notice that Hearing on Petition to Determine value of debtors Real Property, would be held on the 2nd., day of February, 1943, at the hour of Ten O'Clock, A.M., at the office of said Conciliation Commissioner. (That Notice of said Hearing mailed to said Peter J. Wumkes, was returned to this Commissioner with a notation thereon, by the United States Postal Department, "Moved, left no address.")

That a few days prior to the 2nd., day of February, 1943, on the request of Attorneys for said Peter J. Wumkes, said Hearing was by this Commissioner, continued to the 16th day of February, 1943, at Ten O'Clock A. M. And—another continuance requested by said Attorneys, resulted in this Commissioner taking matter off calendar and new Notices of Hearing, mailed to each of the Creditors, by this Commissioner for Wednesday, the 3rd, day of March, 1943. (That by way of explanation, this Commissioner, received a communication from Hon. Garfield R. Jones, Supervising Conciliation Commissioner, that said Peter J. Wumkes, had con-

tacted a Deputy U. S. *States* Attorney, who in turn had contacted Mr. Jones, and then Mr. Jones had contacted said Wumkes and then furnished this Commissioner with the then address of said Peter J. Wumkes.)

That on the 3rd., day of March, 1943, said hearing to determine value of real property was held by this Commissioner, Present at said hearing were debtors, and their attorney Hon. H. R. Griffin, Creditors, Frank G. Clark, and his attorney. Henton S. Brennan, Peter J. Wumkes, and his attorney Russell Goodwin.

That prior to the opening of said hearing and before the appearance in Court of said Peter J. Wumkes, said attorney Russell Goodwin, requested this Commissioner acting as Referee, to allow him, said Goodwin, to withdraw as attorney for said Peter J. Wumkes, which said request was by this Commissioner, denied. At the beginning of said hearing, and before any testimony had been offered, said Goodwin again requested this Commissioner to be [44] allowed to withdraw as attorney for said Peter J. Wumkes, which said request was with the consent of said Peter J. Wumkes, allowed, and granted.

The matter then proceeded to hearing and evidence both documentary and oral was received.

That creditor, Peter J. Wumkes, was present during the taking of all testimony, was, by this Commissioner, asked if he cared to examine each witness produced, was asked if he had any evidence to introduce, in each case he answered in the nega-

tive and refused to ask any witness any questions or to testify himself or produce any evidence.

At the close of the testimony counsel present argued their case respectively and the matter was submitted for decision.

That on the 25th day of March, 1943, this Commissioner rendered his decision fixing value of debtors Real Property and mailed copy of said decision to each creditor present at said hearing and to debtors and attorneys for said debtors and said creditors, appearing.

That on the 2nd., day of April, 1943, Commissioner made his Findings of Fact and Conclusions of Law, in said matter and forwarded by mail to said debtors and to creditors appearing and to attorneys for said debtors and creditors.

That on the 9th day of April, 1943, this Commissioner, signed said Findings of Fact and Conclusions of Law.

That on the 15th day of April, 1943, creditor Frank G. Clark, filed his Petition for Review of the Order of this Commissioner, finding value of Real Property on which he, said Clark, held encumbrance. And on to-wit, the 11th day of May, 1943, said Clark withdrew his Petition for said Review.

That on the 20th day of April, 1943, Peter J. Wumkes, a secured creditor, filed with this Commissioner, *trhough* his attorneys Nichols, Cooper & Hickson, his Petition for Extension of Time to file petition for review, of Commissioner's Order of April, 9th., 1943, To June 1st., 1943, which said petition was granted by said Commissioner. [45]

On May 28th, 1943, Order was entered by Commissioner on request of attorneys for creditor Peter J. Wumkes, for extension of time to file petition for review of Order, dated April, 9, 1943 to June 15th., 1943.

That on June 11th., 1943, said Peter J. Wumkes, filed his petition to Review Conciliation Commissioner's Order of April, 9th, 1943.

SUMMARY OF THE EVIDENCE

Charles Aubrey, a licensed real estate broker and appraiser and until recently District Manager for Farm Security Administration for Riverside, and San Bernardino Counties, former Federal Land Bank appraiser for Southern California, who had appraised Citrus properties in the counties of San Bernardino, Riverside, Ventura, Orange, Los Angeles and other California counties, had appeared as an appraiser before the Federal Court on numerous occasions, fixed the value of debtors real property on which Peter J. Wumkes held encumbrance including water rights, at the sum of $3900.00.

W. H. Johnson, a licensed real estate broker and appraiser, in connection with the Redlands Yucaipa Land Company for Ten years and who had *liver* in or about the city of Redlands for thirty two years, had been engaged in realty and appraisal business for many years, appraising both in this Court and the Superior Court of the state of California, testified that he had gone upon the property mentioned in this petition, had carefully platted a diagram of all the trees situate thereon, that he had spent sev-

eral days in his examination of said property and had taken numerous photographs of the same, which photographs were presented to the Court and introduced in evidence and that he had noticed that the Wumkes grove had been producing between one and a little more than two boxes to the tree with the exception of the years 1941-1942, when said grove produced a little more than three boxes to the tree.

[46]

Mr. Johnson then testified that in his opinion the Wumkes property including the Water Stock was of the value of $3600.00.

That no further oral testimony or evidence was introduced at said Hearing and no request for continuance for the purpose of introducing additional evidence or otherwise was made by any party present. (After the withdrawal of Russell Goodwin, as attorney for Peter J. Wumkes, as hereinbefore shown, this commissioner, said "this is the time and place fixed for the Hearing petition to determine value of debtors real property, are you ready to proceed" no negative answer was interposed.)

I Further Certify, that all Orders of this Court, have been complied with by above named debtors, that all proceeds from crops raised and produced on the real property of debtors, has been deposited with this Commissioner, that all taxes both delinquent and current have been paid.

Question Presented

The question presented by the Petition for Review is:

Is there substantial evidence to sustain the Find-

ings of Fact, Conclusions of Law and Order of the Conciliation Commissioner in fixing the value of the property on which petitioning Creditor holds encumbrance at $3900.00.

Papers Submitted

For the information of the Court, I am herewith submitting the following documents and exhibits.

1. Petition for Reappraisal of Hearing to determine value of debtors Real Property.

2. Notice of Hearing Petition to determine value of debtors Real Property.

3. Notice of Hearing Petition to determine value of debtors real property.

4. Exhibits -1-4-8-9-10-11-12-15-16 and 17, which were exhibits offered pertaining to property subject of this Review. [47]

5. Decision.

6. Findings of Fact and Conclusions of Law.

7. Order Determining Value of Debtors Real Property.

8. Notice of entry of said Order.

9. Petition of creditor Frank G. Clark, to Review Order of Conciliation Commissioner, of April, 9th., 1943, fixing value of debtors real property on which said Frank G. Clark, holds encumbrance.

10. Withdrawal of Petition for Review, last above mentioned.

11. Petition of Peter J. Wumkes, creditor, for Extension of time to file petition for Review of Order of Conciliation Commissioner, of April, 9th, 1943,

12. Order extending time to file petition for Review, last above mentioned.

13. Order extending time in same matter.

14. Petition of Creditor, Peter J. Wumkes, to Review Order of Conciliation Commissioner, of April, 9th., 1943.

15. Envelope containing Notice of Hearing Petition to determine value of debtors real property, addressed to Peter J. Wumkes, with notation of United States Postal Department, thereon.

Dated July 5th., 1943.

Respectfully submitted.

FRED DUFFY

Conciliation Commissioner-Referee. [48]

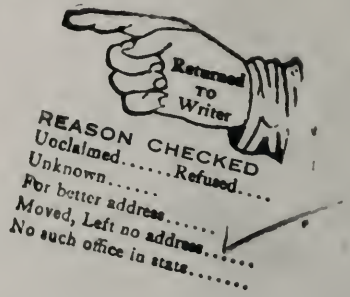
UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA, CENTRAL DIVISION
FRED DUFFY
CONCILIATION COMMISSIONER
318 KATZ BLDG.
SAN BERNARDINO, CALIFORNIA

OFFICIAL BUSINESS

SAN BERNARDINO CALIF. JAN 20 5:30 PM 1943

Penalty for Private Use $300

Peter J. Wunkes -
Redlands
Zone
California



49

[Title of District Court and Cause.]

PETITION TO REVIEW ORDER OF THE CONCILIATION COMMISSIONER UNDER DATE OF APRIL 9, 1943

Comes now your petitioner, Peter J. Wumkes, and respectfully shows:

I.

Petitioner is a secured creditor of the above-named bankrupts, and filed his proof of secured debt in these proceedings, which proof of debt was duly allowed. In this respect your petitioner specifically refers to the said proof of secured debt and incorporates it herein with the same force and effect as though set out in full.

II.

The above-captioned proceedings were instituted on the 25th day of July, 1940, and thereafter the proceedings were referred to Hon. Fred Duffy, United States Conciliation Commissioner for the County of San Bernardino. Thereafter, and on or about the 25th day of October, 1940, the above-named bankrupts filed their amended petition and were duly adjudicated bankrupts under the [50] provisions of Sub-section (s) of Section 75 of the United States Bankruptcy Act. Thereafter, and on or about the 16th day of June, 1941, the said Conciliation Commissioner made and entered his order staying proceedings for a period of three years and setting as rental during such period one-quarter of the gross proceeds of all agricultural in-

come produced on the agricultural real property of the above-named bankrupts, said rent to be paid annually commencing June 16, 1942. In this respect petitioner refers to and incorporates herein the said rent order and order staying proceedings with the same force and effect as though set out in full herein.

III.

Petitioner has not received any rent whatever pursuant to the order set out in Paragraph II above from the Conciliation Commissioner nor from the bankrupts, or either of them, and in this respect petitioner is informed and believes and therefore alleges that the said rent order has not been honored with compliance and is now in default and has at all times mentioned herein been in default.

IV.

On or about the 23rd day of December, 1942, the above-named bankrupts filed a petition requesting a hearing to determine the value of the real property involved in the above-captioned proceedings, and threafter, following several postponements, said petition came on for hearing before the said Conciliation Commissioner. At the time of the said hearing but prior to the introduction of any evidence therein, your petitioner's attorney requested the Conciliation Commissioner's permission to withdraw from the case and thereupon did withdraw from the case, leaving your petitioner unrepresented in the reappraisal proceedings which then followed. In this connection, and through the circumstances of

the withdrawal of petitioner's attorney, as aforesaid, petitioner [51] was not afforded an opportunity of presenting appropriate evidence regarding the true value of the real property concerned in these proceedings.

V.

Thereafter and on or about the 9th day of April, 1943, Hon. Fred Duffy, United States Conciliation Commissioner for San Bernardino County, made and entered his order determining the value of the property securing your petitioner's claim herein at $3900.00, which said order is erroneous in the following respects and particulars:

1. At the time said order of April 9, 1943, was made, the bankrupts, and each of them, were in default of the certain rent order heretofore made and entered in these proceedings.

2. The evidence was insufficient to support the findings of fact, and the findings of fact were in turn insufficient to support the conclusion that the value of the property securing your petitioner's claim was $3900.00.

3. It was illegal, inequitable and improper for the Court to conduct the hearing on the petition for reappraisal at a time when your petitioner was unrepresented by counsel and totally unprepared to present evidence appropriate to establish the actual value of the real property securing your petitioner.

Wherefore, your petitioner, feeling aggrieved by the provisions of said order of April 9, 1943, prays that it may be reviewed as provided by the Bank-

ruptcy Act and amended, modified or set aside in such respects as to the Court seems meet and equitable.

Respectfully submitted,
PETER J. WUMKES
Petitioner.

NICHOLS, COOPER & HICKSON
By DONALD P. NICHOLS
Attorneys for Petitioner.

[Endorsed]: Filed 6/11/43. Fred Duffy, Council Comm. [52]

[Title of District Court and Cause.]

ORDER EXTENDING TIME FOR FILING PETITION FOR REVIEW

It Is Hereby Ordered that the time for filing Petition for Review of the Order determining the value of real property entered on the 9th day of April, 1943, be, and the same is hereby extended to June 15th, 1943.

Dated this 28th day of May, 1943.
FRED DUFFY
Conciliation Commissioner for
San Bernardino County,
California [53]

[Title of District Court and Cause.]

CERTIFICATE EXTENDING TIME FOR FILING PETITION FOR REVIEW

The petition of Peter J. Wumkes, creditor of the above-named debtors, having been filed and good cause appearing therefor

It Is Hereby Ordered that the time for filing a petition for review of the order determining value of real property entered on the 9th day of April, 1943 be and the same is hereby extended to June 1st, 1943.

Dated this 20th day of April, 1943.

FRED DUFFY
Conciliation Commissioner for
San Bernardino County,
California

DPN:B

[Endorsed]: Recd. and filed. Filed. Fred Duffy, Council Comm. [54]

[Title of District Court and Cause.]

PETITION FOR CERTIFICATE EXTENDING TIME FOR FILING PETITION FOR REVIEW

Comes now Peter J. Wumkes, one of the secured creditors of the above-named Debtors, and respectfully represents as follows:

I.

That on the 9th day of April, 1943, the Honorable Fred Duffy, Conciliation Commissioner and Referee

of the above entitled Court, regularly entered his order determining the value of the above Debtors' real property.

II.

That your petitioner has filed a petition for authority to re-open the hearing to determine value and be permitted to introduce evidence as to the actual value of said property.

III.

That the hearing on said petition has been set for a date in the future and your petitioner desires that the time be extended for filing a petition for review so as to permit your petitioner to have until June 1, 1943, to file his petition for review or appeal.

Wherefore, your petitioner prays that an order be made extending the time as in this petition requested.

PETER J. WUMKES
Petitioner.

NICHOLS, COOPER & HICKSON
Attorneys for Petitioner. [55]

State of California,
County of Los Angeles.—ss.

Peter J. Wumkes, being by me first duly sworn, deposes and says:— That he is the petitioner in the foregoing and above entitled action; that he has read the foregoing Petition for Certificate Extending Time for Filing Petition for Review and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are

therein stated upon his information or belief, and as to those matters that he believes it to be true.

PETER J. WUMKES

Subscribed and sworn to before me this 15th day of April, 1943.

[Seal] ALICE M. KESTERSEN

Notary Public in and for the County of Los Angeles, State of California.

[Endorsed]: Recd. and Filed 4/20/43. Fred Duffy, Council Comm. [56]

Henton S. Brenan
Attorney At Law
203-204 Security First National
Bank Building
Phone 4755
Redlands, California

May 11, 1943

Fred Duffy
Conciliation Commissioner
San Bernardino, Calif.

Re: James Goodwin Powell No. 36775-C

Dear Sir:

This letter is to inform you that we do not intend to pay the filing fee required to file our petition for a hearing on review by the creditor Frank Clark, and that you may withdraw the petition from your files.

Very truly yours,

b/p HENTON S. BRENAN [57]

[Title of District Court and Cause.]

PETITION FOR REVIEW OF ORDER OF CONCILIATION COMMISSIONER

To The Honorable Fred Duffy, as Conciliation Commissioner of the Above Entitled District Court, In and For the County of San Bernardino, State of California:

The petition of Frank G. Clark, respectfully represents:

That your petitioner is a creditor of the above named debtor;

That your petitioner is a creditor by virtue of being the owner and holder of a certain promissory note executed by the debtors and secured by a deed of trust upon the real property described in the order hereinafter referred to; that the claim upon the balance due on said promissory note in the amount of approximately $8221.62 has been allowed as a secured claim.

That on the 9th day of April an order was made and entered in the above entitled proceeding, a copy of which is hereto annexed and made a part hereof;

That by said order it is determined that the property described in said deed of trust and constituting the security for the indebtedness evidence by said promissory note, is of the value of $3525.00;

That said order was and is erroneous for the following reasons:

a. That the valuation of the property aforesaid was and is the sum of $6050.00. [58]

b. Said order and the valuation of said property thereby fixed are contrary to the evidence, in that:

1. The witness Charles Aubrey, appraiser for the debtor appraised the property of a value of $4150.00,

2. The witness W. H. Johnson appraiser for the debtor appraised the property as of a value of $3525.00,

3. The witness J. D. Inman, appraiser for the creditor herein appraised the property as of a value of $6050.00,

4. The witness James Wheat appraiser for the creditor herein appraised the property as of a value of $5500.00,

c. Said order and the valuation thereby fixed are not supported by the evidence.

Wherefore your petitioners pray that the said order may be reviewed by a Judge of this Court, as provided in the Acts of Congress relating to bankruptcy.

Dated this 14 day of April, 1943.

FRANK G. CLARK

State of California
County of San Bernardino

Frank G. Clark, being first duly sworn, deposes and says:

That he is the petitioner in the above petition; that he has read the foregoing petition and knows the contents of the same; that the same is true of his own knowledge, except as to those matters stated

therein on information and belief, and as to such matters he believes it to be true.

FRANK G. CLARK

Subscribed and sworn to before me this 14 day of April, 1943.

TERESA A. MILLER
Notary Public in and for said County and State

[Endorsed]: Filed 4/15/43. Fred Duffy, Council Comm. [59]

[Title of District Court and Cause.]

ORDER DETERMINING VALUE OF DEBTOR'S REAL PROPERTY

The petition of the above named debtors requesting a court reappraisal or hearing to determine the value of debtors' real property, coming on regularly for hearing on the 2nd day of February, 1943, and upon the request of Attorney J. C. Sexton was duly and regularly continued until February 16, 1943, and again upon the request of said J. C. Sexton, until March 3, 1943, and on March 3, 1943 at the hour of 10:00 A. M. thereof, before the Honorable Fred Duffy, Conciliation Commissioner of the above entitled Court in and for the County of San Bernardino, State of California, appeared said debtors personally and through their Attorney, H. R. Griffin, Esq., and Frank G. Clark, personally, and through his attorney, Hempton S. Brenan, Esq., and Peter J. Wumkes, personally, and through his Attorney, Russell Goodwin, Esq.; that theretofore

said Russell Goodwin had requested the court to allow him to withdraw as attorney for the said Peter J. Wumkes, and said request had been denied, which said request was renewed upon the opening of said hearing and said Russell Goodwin was permitted to withdraw as attorney with the consent and approval of the said Peter J. Wumkes; and no appearance being made either in person or by counsel for any other creditor scheduled in the above-entitled proceeding; and evidence both oral and documentary having been introduced and witnesses examined on behalf of the debtors and the appearing creditors, and said [60] hearing having been concluded and the cause having been argued by respective counsel and submitted, and the court having duly made and entered its Findings of Fact and Conclusions of Law,

Now Therefore It Is Hereby Ordered, Adjudged and Decreed:

I.

That the value of Peter J. Wumkes' portion of the property on which the said Peter J. Wumkes has an encumbrance is of the value of $3,900.00.

II.

That the value of the property on which Frank C. Clark holds an encumbrance is of the value of $3,525.00.

III.

That the value of the entire property is the sum of $7425.00.

IV.

That said debtors may redeem said property by paying into Court said sum of $7,425.00 on or before the 16th day of June, 1944, of which sum of $3,900.00 shall be paid to Peter J. Wumkes and the sum of $3525.00 to said Frank J. Clark; provided, however, in case the order fixing value is appealed from debtors may redeem by paying into court, the said sum of $7425.00 within three months from and after the date said Order on Appeal becomes final, and provided further, that in the event of the period of three months from and after the date *of* said Order on Appeal, becomes final, expires prior to the 16th day of June, 1944, debtors may have until the 16th day of June, 1944 to redeem said property by paying said sum of $7425.00 into this court.

Provided further, that debtors, since they have retained possession of the properties involved in this hearing, they will be required to redeem both pieces of property if redemption is made.

Dated this 9th day of April, 1943.

(Signed) FRED DUFFY

Conciliation Commissioner-Referee [61]

[Title of District Court and Cause.]

NOTICE OF ENTRY OF ORDER DETERMINING VALUE OF DEBTORS' REAL PROPERTY

To the Creditors of James Goodwin Powell and Anna Strachan Powell, of Redlands, San Bernardino County, and District and State Aforesaid, Bankrupts:

Notice Is Hereby Given that on the 9th day of April, 1943, the Honorable Fred Duffy, Conciliation Commissioner and Referee of the above-entitled Court, did duly and regularly enter his Order Determining the Value of Said Debtors' Real Property.

Dated this 9th day of April, 1943.

FRED DUFFY
Conciliation Commissioner-
Referee.

[Endorsed]: Filed 4/9/43. Fred Duffy, Council Comm. [62]

[Title of District Court and Cause.]

ORDER DETERMINING VALUE OF DEBTORS' REAL PROPERTY

The Petition of the above-named debtors requesting a court reappraisal or hearing to determine the value of debtors' real property, coming on regularly for hearing on the 2nd day of February, 1943, and upon the request of Attorney J. C. Sexton was

duly and regularly continued until February 16, 1943, and again upon the request of said J. C. Sexton, until March 3, 1943, and on March 3, 1943 at the hour of 10:00 A. M. thereof, before the Honorable Fred Duffy, Conciliation Commissioner of the above-entitled court in and for the County of San Bernardino, State of California, appeared said debtors personally and through their Attorney, H. R. Griffin, Esq., and Frank G. Clark, personally, and through his Attorney, Hempton S. Brenan, Esq., and Peter J. Wumkes, personally, and through his Attorney, Russell Goodwin, Esq.; that theretofore said Russell Goodwin had requested the court to allow him to withdraw as attorney for the said Peter J. Wumkes and said request had been denied, which said request was renewed upon the opening of said hearing and said Russell Goodwin was permitted to withdraw as attorney with the consent and approval of the said Peter J. Wumkes; and no appearance being made either in person or by counsel for any other creditor scheduled in the above-entitled proceeding; and evidence both oral and documentary having been introduced and witnesses examined on behalf of the debtors and the appearing creditors, and said hearing [63] having been concluded and the cause having been argued by respective counsel and submitted, and the court having duly made and entered its Findings of Fact and Conclusions of Law.

Now, Therefore, It Is Hereby Ordered, Adjudged and Decreed:

I.

That the value of Peter J. Wumkes' portion of the property on which the said Peter J. Wumkes has an encumbrance is of the value of $3,900.00.

II.

That the value of the property on which Frank C. Clark holds an encumbrance is of the value of $3,525.00.

III.

That the value of the entire property is the sum of $7,425.00.

IV.

That said debtors may redeem said real property by paying into court said sum of $7,425.00 on or before the 16th day of June, 1944, of which sum of $3,900.00 shall be paid to Peter J. Wumkes and the sum of $3,525.00 to said Frank J. Clark; provided, however, in case the order fixing value is appealed from debtors may redeem by paying into court, the said sum of $7,425.00 within three months from and after the date said Order on Appeal becomes final, and provided further, that in the event of the period of three months from and after the date said Order on Appeal, becomes final, expires prior to the 16th day of June, 1944, debtors may have until the 16th day of June, 1944 to redeem said property by paying said sum of $7,425.00 into this court.

Provided further, that debtors, since they have retained possession of the properties involved in this hearing, they [64] will be required to redeem both pieces of property if redemption is made.

Dated this 9th day of April, 1943.

FRED DUFFY
Conciliation Commissioner-
Referee.

[Endorsed]: Filed 4/9/43. Fred Duffy, Council Comm. [65]

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The Petition of the above-named debtors requesting a court reappraisal or hearing to determine the value of debtors' real property, coming on regularly for hearing on the 2nd day of February, 1943, and upon the request of Attorney J. C. Sexton was duly and regularly continued until February 16, 1943, and again upon the request of said J. C. Sexton, until March 3, 1943 and on March 3, 1943 at the hour of 10:00 A. M. thereof, before the Honorable Fred Duffy, Conciliation Commissioner of the above-entitled court in and for the County of San Bernardino, State of California, appeared said debtors personally and through their Attorney, H. R. Griffin, Esq., and Frank G. Clark, personally, and through his Attorney, Hempton S. Brenan, Esq., and Peter J. Wumkes, personally, and through his Attorney, Russell Goodwin, Esq.; that theretofore said Russell Goodwin had requested the court to allow him to withdraw as attorney for the said Peter J. Wumkes and said request had been denied,

which said request was renewed upon the opening of said hearing and said Russell Goodwin was permitted to withdraw as attorney with the consent and approval of the said Peter J. Wumkes; and no appearance being made either in person or by counsel for any other creditor scheduled in the above-entitled proceeding; and evidence both oral and documentary having been introduced and witnesses examined on behalf of the debtors and the appearing creditors, and said hearing [66] having been concluded and the cause having been argued by respective counsel and submitted, and the court being fully advised of the law in the premises, and after due consideration and deliberation thereon, makes its Findings of Fact as follows:

FINDINGS OF FACT

I.

The court finds that said debtors on or about the 25th day of July, 1940, filed their joint Petition in the above-entitled court, praying for relief as provided for in Section 75 of the Bankruptcy Act; that the filing of said Petition was approved by the above-entitled court and referred to Fred Duffy, Esq., Conciliation Commissioner, for further proceedings.

II.

That on or about the 25th day of October, 1940, said petitioners having been unable to secure acceptance or confirmation of their extension proposal, filed their amended Petition and were adjudicated bankrupts in accordance with the provisions of Sec-

tion 75(s) of the Bankruptcy Act, and that the above-entitled matter was referred to the Honorable Fred Duffy, Conciliation Commissioner, for further proceedings; and that thereafter and on the 16th day of June, 1941, said Honorable Fred Duffy, Conciliation Commissioner, made and entered an order setting aside the exempt properties to said debtors, giving said debtors possession of their properties for a period of three years, and setting the rental to be paid by said debtors.

III.

That the court further finds that scheduled by said debtors in their schedules was the following described real property owned by said debtors and situated in the County of San Bernardino, State of California, and more particularly described as follows, to-wit: [67]

Parcel 1: That property in the City of Redlands, County of San Bernardino, State of California, described as:

That portion of the Northwest quarter of the Southeast quarter of Section 21, Township 1 South, Range 3 West, San Bernardino Base & Meridian, described as: Beginning on the North line of said Northwest quarter of Southeast quarter 1008.87 feet East of the Northwest corner of said Southeast quarter: thence South along the East line of land of Israel Beal, 853.33 feet to a point 466.67 feet North of the South line of said Northwest quarter of the Southeast quarter; thence West 342 feet;

thence North and parallel with first course herein (853.33 feet; thence East 342 feet to beginning; Except that portion conveyed to the Lugo Water Company by Deed recorded in Book 438 of Deeds, at page 384 described as follows: Commencing at the Northeast corner of the Southeast ¼ of said section; thence West along the center line of Lugonia Avenue, 1716 feet for point of beginning; thence South 0 degrees 12′ East 48 feet; thence West 55 feet; thence North 0 degrees 12′ West 48 feet; thence East 55 feet to the place of beginning. Together with Four (4) shares of the capital stock of the Lugo Water Company, a corporation.

Parcel 2: That property in the City of Redlands, County of San Bernardino, State of California, described as:

All that portion of the Northwest quarter of the Southeast quarter of Section 21, Township 1 South, Range 3 West, San Bernardino Base & Meridian, in the City of Redlands, according to Government Survey, described as follows:

Beginning at a point on the East boundary line of the above described tract, which is 718.07 feet North from the Southeast corner thereof; thence running North along the East boundary line thereof 597.08 feet, more or less, to the Northeast corner of said tract; thence West along the North boundary line thereof, 311.13 feet, more or less, to a point which is 1,008.87 feet East from the Northwest corner of said tract; thence Southerly on a line parallel with

the East boundary of said tract 597.08 feet, more or less, to a point due West of the point of beginning; thence East 311.13 feet, more or less, to the beginning.

Together with 5 shares of the capital stock of the Lugonia Water Company, a corporation.

IV.

That the court finds that on or about the 23 day of December, 1942, the said petitioners filed their joint [68] Petition requesting reappraisal or hearing to determine value of debtors' real property; that pursuant to said Petition, a meeting of the creditors was called by the Honorable Fred Duffy, Conciliation Commissioner, to hear and determine the value of the debtors' real property.

V.

That the court further finds that the debtors' real property consists of two parcels of land as described in Paragraph III, hereof, and is entirely planted to Citrus, with the exception that there is located on the Clark property a small house approximately 24 feet x 36 feet, together with a garage 18 feet x 24 feet, and an unoccupied poultry building 18 feet x 48 feet, that the Clark property consists of approximately 4.2 acres, and the Wumkes' property adjoins said Clark's property and consists of approximately 5-7/8ths. acres.

VI.

The court further finds that the Clark property is planted to approximately 484 trees; that a num-

ber of said trees are Sweets, Blood Oranges and Australian Orange trees; that said Australian trees are large trees, as indicated by the exhibit on file. but are not productive and that there is less than a box of oranges on the tree, as shown in the exhibit; that the remainder of said grove consists of trees approximately 40 years old, but that 4 rows have been replanted, which trees are now approximately 10 years old and are not well developed. That as you travel from the front of said grove back towards the rear, there is to be noted increasing signs and indications that a stream or wash has traversed the rear portion of the grove, and this condition of the soil is reflected in the poor condition of the grove; that said grove is furnished with water, as represented by 5 shares of Bear Valley Company's stock, and that said [69] stock is hardly sufficient for the needs of that grove.

VII.

That the court further finds that the Wumkes' grove is planted to approximately 798 trees, being divided as follows: approximately 95 young Valencia trees, being 8 to 9 years old, 399 old Valencia trees and 304 Navel trees; that these trees are set too closely together, and this property, like the Clark property, has a gravelly soil, which soil becomes very noticeable as you travel towards the rear of the grove, and the condition of the trees reflect the poor condition of the soil. The Wumkes' grove is supplied with water, as represented with 4 shares of Lugo water.

VIII.

That the court finds that the house situated upon the Clark grove is in considerable need of repair.

IX.

The court further finds that the production of Citrus fruit is the highest and best use for said real property.

X.

The court further finds that the grove has had proper care and attention and the poor condition of the grove is directly attributable to the poor condition of the soil and the original selection of trees planted upon the property. The court further finds that the crop records are available, and commencing with the year 1935-1936, show as follows:

	CLARK		WUMKES	
1935-1936	1,165 boxes	$ 878.35		
1936-1937	1,042 "	930.26	872 boxes	$1,578.15
1937-1938	843 "	259.94	991 "	387.39
1938-1939	1,136 "	304.02	1,958 "	764.72
1939-1940	1,001 "	558.18	1,983 "	1,261.16
				[70]
1940-1941	1,187 "	617.32	1,616 "	1,306.87
1941-1942	1,827 "	974.63	3,061 "	3,287.06

XI.

That there has been picked in this year, 416 boxes from the Clark grove and 263 boxes from the Wumkes' grove, and that it is estimated that there are approximately 70 boxes additional on the Clark grove and approximately 305 boxes on the Wumkes' grove, and the court further finds that the current crop in this locality is very light.

XII.

The court finds that the total value of the Wumkes' property is the sum of $3,900.00.

XIII.

The court further finds that the value of the Clark property, including the grove, house, buildings and water stock, is of the total value of $3,525.00.

XIV.

The court further finds that the total value of the Wumkes' property involved and the Clark property invovlved is the sum of $7,425.00.

XV.

That the witnesses testifying in the above hearing and the value of the property, in their opinion, is set out as follows:

Charles Aubrey, a Licensed Real Estate Broker and Appraiser, and, until recently, District Manager for the Farm Security Administration for Riverside and San Bernardino Counties; a former Federal Land Bank Appraiser for Southern California; a Real Estate Broker, and who has appraised Citrus properties in San [71] Bernardino, Riverside, Ventura, Orange and Los Angeles, and other California counties, and an appraiser who has appeared before the Federal Court and this Court, testified that the Clark Grove consisted of 4.2 acres with 493 trees planted thereon, that many of said trees were Sweets, Bloods and Australians, and the remainder of said trees were from 40 to 50 years old, excepting 4 rows of trees averaging from 10 to 12 years of

age; that the Wumkes' grove consisted of 5-7/8ths acres planted to approximately 798 trees, being divided approximately as follows: 95 young Valencia trees from 8 to 9 years old, 399 old Valencia trees and 304 Navel trees. That the soil of both groves is sandy loam with gravelly spots, except approximately 4 acres which are very gravelly; that the trees are set too close together and by reason of the soil, it has not produced very satisfactorily, the crop records showing that the entire 10 acres is a marginal producer; that the land, however, is best adapted to Citrus production and that, in his opinion, the irrigation water supply is not quite adequate. Mr. Aubrey testified that in his opinion, and after going over the property very thoroughly, and the crop records, that the Wumkes' property was worth $650.00 an acre, including water, or a total of $3,900.00 That the Clark grove, including the house, garage, poultry building and water stock, is worth the sum of $4,150.00. And he appraised the house in this grove at the sum of $1,800.00, $100.00 for the garage and $250.00 for the poultry building.

W. H. Johnson, a Licensed Real Estate Broker and Appraiser in connection with the Redlands Yucaipa Land Company for 10 years, and who has lived in or about the City of Redlands for 32 years and has been engaged in the Realty and Appraisal business for many years, appraising both in this Court and the Superior Court of the State of California, testified that he had gone upon each of the properties and had carefully platted upon a diagram

all of the trees situate thereon, and that he had spent several [72] days in his examination of said properties and had taken numerous photographs of the same, which photographs were presented to the court and introduced in evidence, and that he had noted that the Clark grove had planted a number of Blood, Sweet and Australian trees, and that the condition of the soil towards the rear of both of said groves was very gravelly and indicated the former existence of a wash or stream, and that this condition of the soil had caused considerable difficulties in the raising and care of the Citrus trees and was reflected in the small size and poor appearance of the trees and the resulting loss of fruit; that he had examined the crop returns and was familiar with them, and that it appeared the Clark grove had been producing between 2 and 3 boxes of oranges to the tree, with the exception of the year 1941-1942 which was an exceptionally heavy bearing year for nearly all groves, when the Clark grove produced slightly more than 4 boxes to a tree and that the Wumkes' grove had been producing between one and a little more than 2 boxes to the tree, with the exception of the same year of 1941-1942 when it likewise produced a little more than 3 boxes to the tree. That he had examined and gone through the dwelling house located upon the Clark property and that he found that it was in considerable need of repair and that he had examined the garage and chicken house. Mr. Johnson then testified that, in his opinion, the Wumkes' property, including water stock, was worth $3,600.00, and the Clark property,

including all buildings and water stock, $3,525.00.

James Goodwin Powell testified that he was the owner of the property and that he had resided thereon for a number of years and testified that the house was approximately 26 x 32 feet with a small living room and dining room approximately 11x18 feet and 2 bedrooms, each approximately 11 x 12 feet, and a kitchen and a small bathroom; that the bathroom was approximately [73] 9 x 5 feet with a linoleum floor and a old style bathtub set up on legs rather than enclosed, and he further testified that, in his opinion, the value of both the Wumkes' property and Clark property, together with all buildings and water stock, was in the sum of $7,500.00.

J. D. Inman testified that he has been a Broker in and about the City of Redlands since 1929, that the grove was in an underfed condition and that a portion thereof consisting of approximately 1 acre was gravel, that, in his opinion, the Clark land, water and flumes, was worth $2,200.00, that the trees on the Clark property were worth $1,200.00, and the house thereon was worth $2,100.00, the garage $350.00 and the chicken coop $200.00, thus making a total of $6,050.00. That, in his opinion, the property had increased in value from Ten (10%) to Twenty (20%) Per Cent during the last year.

James Wheat testified that he had been a former Postmaster of the City of Redlands and was now engaged in the Real Estate business; that, in his opinion, the Clark property, buildings and water stock, were worth $5,500.00.

CONCLUSIONS OF LAW

I.

That the value of Peter J. Wumkes' portion of the property on which the said Peter J. Wumkes has an encumbrance is of the value of $3,900.00.

II.

That the value of the property on which Frank G. Clark holds an encumbrance is of the value of $3,525.00.

III.

That the value of the entire property is the sum of $7,425.00. [74]

IV.

That said debtors may redeem said real property by paying into court said sum of $7,425.00 on or before the 16th day of June, 1944, of which sum of $3,900.00 shall be paid to Peter J. Wumkes and the sum of $3,525.00 to said Frank J. Clark; provided, however, in case the order fixing value is appealed from debtors may redeem by paying into court, the said sum of $7425.00 within three months from and after the date said Order on Appeal becomes final, and provided further, that in the event of the period of three months from and after the date said Order on Appeal, becomes final, expires prior to the 16th day of June, 1944, debtors may have until the 16th day of June, 1944 to redeem said property by paying said sum of $7,425.00 into this court.

Provided further, that debtors, since they have retained possession of the properties involved in

this hearing, they will be required to redeem both pieces of property if redemption is made.

Dated this 9th day of April, 1943.

FRED DUFFY
Conciliation Commissioner-
Referee.

[Endorsed]: Filed 4/2/43. Fred Duffy, Council Comm. [75]

[Title of District Court and Cause.]

DECISION

This matter coming on to be heard on petition of debtors to determine value of real property.

Debtors appearing personally and by H. R. Griffin, their attorney. Creditors, appearing were Frank G. Clark, holder of Trust Deed on one piece of property, personally and by his attorney, Henton S. Brenan, and Peter J. Wumkes, holder of Trust Deed on one piece of property, and his attorney, Russell Goodwin. That said attorney asked the court to allow him to withdraw as attorney for said Peter J. Wumkes, said request was denied, but before the Hearing said Russell Goowwin did withdraw as attorney with the consent and approval of said Peter J. Wumkes.

Above entitled matter was set for Hearing for the 2nd., day of February, 1943, and at the request of attorneys for creditors, matter was continued to February, 16th., 1943. And on request of creditors

attorneys, was again continued to March, 3rd., 1943., at which time matter was heard.

At said Hearing the Court, received evidence both oral and documentary.

After considering all the evidence, I have reached the conclusion that the value of debtors real property is as follows:

That the value of the Peter J. Wumkes portion or the property on which said Peter J. Wumkes, has encumbrance is of the value of $3900.00.

That the value of the property on which Frank G. Clark, holds encumbrance is of the value of $3525.00.

That the value of the entire property is the sum of $7425.00. Debtors may redeem said real property by paying into Court, the [76] said sum of $7425.00, on or before the 16th day of June, 1944. Of which sum $3900.00, shall be paid to Peter J. Wumkes, and the sum of $3525.00, to said Frank G. Clark.

Provided However, in case Order fixing value is appealed from debtors may redeem by paying into Court, the said sum of $7425.00, within three months from and after the date said Order on Appeal, becomes final.

Provided Further, that in the event the period of three months from and after the date said Order on Appeal, becomes final, expires prior to the 16th day of June, 1944, debtors may have until the 16th day of June, 1944, to redeem said property by paying said sum of $7425.00 into this Court.

It is my view, that debtors, since they have re-

tained possession of properties involved in this Hearing, they will be required to redeem both pieces of said property if redemption is made.

Attorney for petitioning debtors, will prepare appropriate Findings, Conclusions and Order.

Dated San Bernardino, California, this 25th day of March, 1943.

FRED DUFFY
Conciliation Commissioner-
Referee [77]

Scale

N N N N N N N N

S S S S S S S S

S S S S S S S S

S S S S S S S S

S S S A S S S S

yard

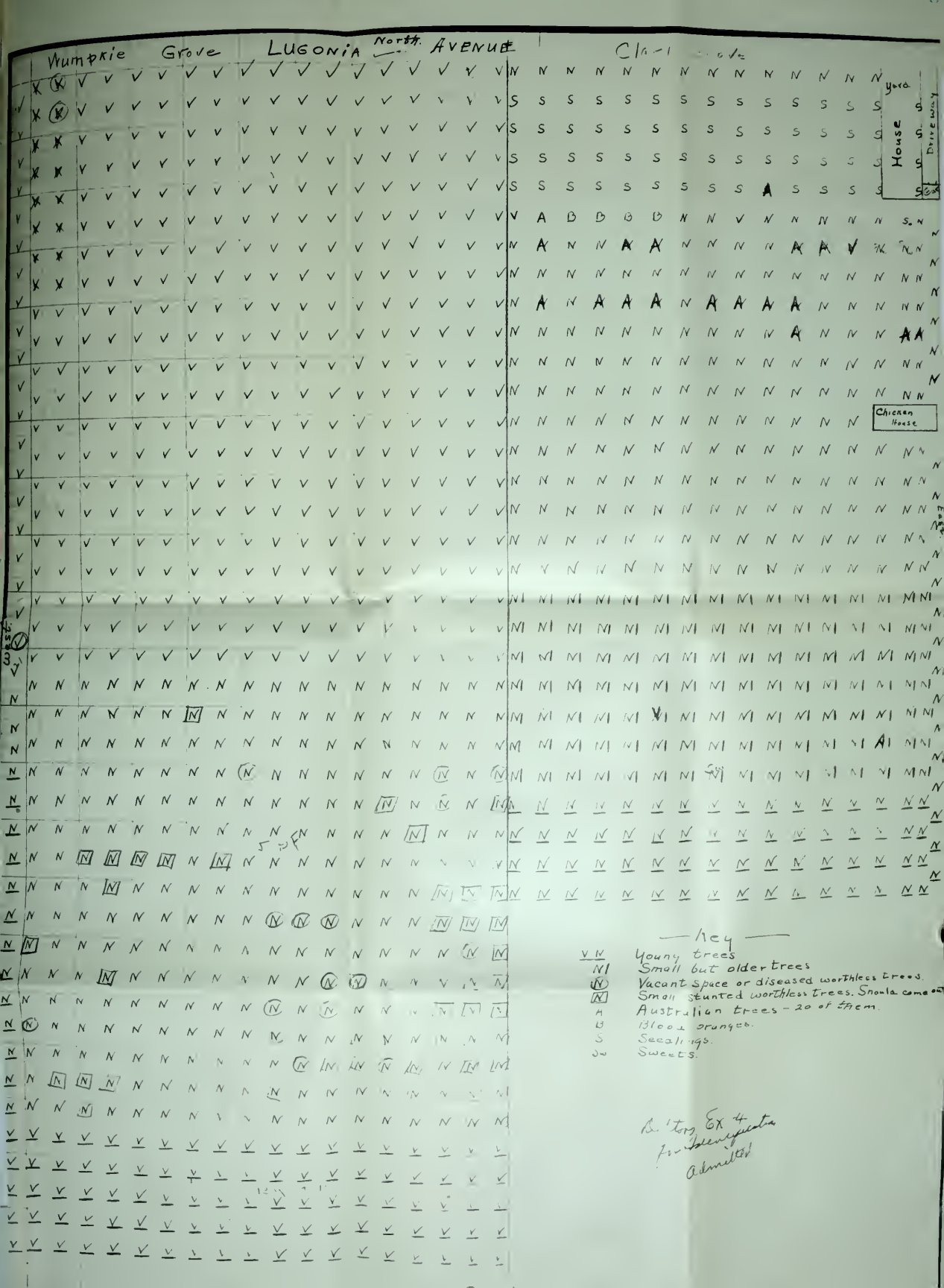
House

Driveway

Gate

tunted worthless trees. Should come out
lian trees - 20 of them.
oranges.
gs.

Ex 4
Identification
Admitted


Wumpkie Grove
LUGONIA North AVENUE
Chicken House
Yard
House
Driveway
Key
Young trees
Small but older trees
Vacant Space or diseased worthless trees.
Small stunted worthless trees. Snails come on
Australian trees - 20 of them.
Blood oranges.
Seedlings.
Sweets.
Re Items Ex 4 for identification admitted

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif., Aug 12 32
Pool No.—One Variety—Valencias
From—Beginning of Season to June 30

Grower—J G Powell
Address—Redlands

Record of Fruit Received

Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	Credits FIRST GRADE			Amount	Totals
						80		Per Box			
une 3	18356	60				100	@ $1.8440	"	"		
					1	126	@ 2.0296	"	"	2 03	
					3	150	@ 1.9022	"	"	5 70	
					4	176	@ 1.6550	"	"	6 62	
					6	200	@ 1.3161	"	"	7 89	
					8	216	@ 1.0332	"	"	8 26	
					5	252	@ .9185	"	"	4 59	
					4	288	@ .8234	"	"	3 29	
					2	344	@ .7224	"	"	1 44	
						392	@ .6356	"	"		
						Jumbles					
					33	Total					39 82
							SECOND GRADE				
						80		Per Box			
						100	@ $ .8012	"	"		
						126	@ .9567	"	"		
						150	@ 1.0127	"	"		
						176	@ .9685	"	"		
						200	@ .8141	"	"		
					1	216	@ .6371	"	"	63	
					1	252	@ .4279	"	"	42	
					1	288	@ .3237	"	"	32	
						344	@ .3121	"	"		
						392	@ .3059	"	"		
						Jumbles					
					3	Total					1 37
					36	Total Packed Boxes					
					73#	Standards Sold Loose	@$ 4040 Cwt.				29
						Culls Sold Loose					
					80#	Culls Processed					
						Culls Worthless					
						Gross Returns					41 48

Statement of Account

	Debit	Credit
Gross Returns This Pool		41 48
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	4 20	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	3 24	
Growers Supplies Purchased		
Cash Advances		
Credit to Account		
Balance Due		
Check to Balance	34 04	
Total	41 48	41 48

Your pool average is $1 15 per packed box
In Addition there will be a Cash Fund estimated at $ 15 per packed box

Total Average $1 30 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

[Pencilled] : 1932
Grower—J G Powell
Address—Redlands

Redlands, Calif., May 17 32
Pool No.—Three
From—Jan 16 to Mar 15

Variety—Naels

Record of Fruit Received				Credits						
Date	Ticket No.	Field Boxes	√ Weight	Boxes	Size		FIRST GRADE		Amount	Totals
				11	80	@	$ .7473	Per Box	8 22	
				36	100	@	.8034	" "	28 92	
Feb 23	17244	65		68	126	@	.8381	" "	56 99	
24	17261	72		73	150	@	1.0044	" "	73 32	
	17270	72		53	176	@	1.2006	" "	63 63	
	17272	72		38	200	@	1.5237	" "	57 90	
	17274	72		31	216	@	1.4045	" "	43 54	
	17275	64		18	252	@	1.4191	" "	25 54	
Mar 17	17564	72		14	288	@	1.3437	" "	18 81	
	17568	72		4	344	@	1.1955	" "	4 78	
	17574	72			392	@	1.1158	" "		
	17 76	72			Jumbles					
	17577	72								
18	17579	69		346	Total					381 65
	17580	72		4	80	@	$ .2581	Per Box	1 03	
				7	100	@	.2742	" "	1 92	
		918		19	126	@	.3951	" "	7 50	
				20	150	@	.4885	" "	9 77	
				22	176	@	.6134	" "	13 49	
				22	200	@	.7489	" "	16 47	
				19	216	@	.8706	" "	16 54	
				10	252	@	.8874	" "	8 87	
				7	288	@	.8905	" "	6 23	
				4	344	@	.7991	" "	3 19	
Note: Fruit Inclined To Be Large, and Coarse, Somewhat Thrip Marked and Stem End Spotted.				1	392	@	.6691	" "	67	
					Jumbles					
				135	Total					85 68
				481	Total Packed Boxes					
				6677#	Standard Sold Loose @ $ .4320 Cwt.					28 84
[In pencil]:					Culls Sold Loose					
3 22				1420#	Culls Processed					
34 04				840#	Culls Worthless					
64 55										
3 61					Gross Returns					496 17
6 43										
111.85										

Statement of Account

	Debit	Credit
Debtors Ex 17		
Gross Returns This Pool		496 17
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	55 07	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	43 29	
Growers Supplies Purchased		
Tankage	75 00	
Cash Advances		
Credit to Account		
Balance Due		
Check to Balance	322 81	
Total	496 17	496 17

Your pool average is $1 03 per packed box
In Addition there will be a Cash Refund estimated at $ 15 per packed box

Total Average $1 18 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.,—June 28 32
Grower—J G Powell
Address—Redlands
Pool No.—Season
Variety—Seeds
From..... To.....

Record of Fruit Received					Credits						
Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	FIRST GRADE			Amount	Totals
						80		Per Box			
						100					
Feb 23	17228	64				126	@ $ .7803	"	"		
	17231	44			2	150	@ .8802	"	"	1 76	
	17243	44			4	176	@ .9411	"	"	3 76	
					8	200	@ 1.0229	"	"	8 18	
		152			13	216	@ 1.0570	"	"	13 74	
					16	252	@ 1.0553	"	"	16 88	
					21	288	@ 1.0605	"	"	22 27	
					11	344	@ .7514	"	"	8 26	
					7	392	@ .7149	"	"	5 00	
						Jumbles					
					82	Total					79 85
							SECOND GRADE				
						80		Per Box			
						100	@ $ .2145	"	"		
						126	@ .2145	"	"		
						150	@ .2828	"	"		
						176	@ .4006	"	"		
						200	@ .4652	"	"		
					1	216	@ .5104	"	"	51	
					2	252	@ .5511	"	"	1 10	
					3	288	@ .4828	"	"	1 45	
					2	344	@ .2882	"	"	57	
						392	@ .2064	"	"		
						Jumbles					
					8	Total					3 63
					90	Total Packed Boxes					
						Standards Sold Loose @ $ .4000 Cwt.					
						Culls Sold Loose					
					560#	Culls Processed					
					120#	Culls Worthless					
						Gross Returns					83 48

Statement of Account

	Debit	Credit
Gross Returns This Pool		83 48
New Returns on Bloods		3 61
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	14 44	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	8 10	
Growers Supplies Purchased		
Cash Advances		
Credit to Account		
Balance Due		
Check to Balance	64 55	
Total	87 09	87 09

Your pool average is $ 93 per packed box
In Addition there will be a Cash Refund estimated at $ 15 per packed box

Total Average $1 08 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.,—June 28 32
Grower—J G Powell
Address—Redlands
Pool No.—Season Variety—Bloods
From..... To.....

Record of Fruit Received

Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	Credits FIRST GRADE			Amount	Totals
						80		Per Box			
						100					
Feb 23	17242	12				126					
						150					
						176					
						200					
						216					
					1	252	@	$1.3600	" "	1 36	
					2	288	@	1.2873	" "	2 57	
					1	344	@	.6285	" "	63	
					1	392	@	.5872	" "	58	
						Jumbles					
					5	Total					5 14
							SECOND GRADE				
						80		Per Box			
						100					
						126					
Notes—Sizes Quite Small						150					
						176					
						200					
						216					
						252					
						288					
						344					
						392					
						Jumbles					
					5	Total Packed Boxes					
						Standards Sold Loose					
						Culls Sold Loose					
					170#	Culls Processed					
						Culls Worthless					
						Gross Returns					5 14

Statement of Account

	Debit	Credit
Gross Returns This Pool		5 14
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	1 08	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	45	
Growers Supplies Purchased		
Cash Advances		
Credit to Account	3 61	
Balance Due		
Check to Balance		
Total	5 14	5 14

Your pool average is $1 03 per packed box
In Addition there will be a Cash Refund estimated at $ 15 per packed box

Total Average $1 18 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Aug 12 32

Grower—J G Powell
Address—Redlands

Pool No.—Two
From—June 1 to June 30

Variety—Local Grapefruit

Record of Fruit Received					Credits						
Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size				Amount	Totals
						36	FIRST GRADE		Per Box		
June 9	18357	13				48					
					1	64	@ $1.1789	"	"	1 18	
					2	80	@ 1.1110	"	"	2 22	
					2	100	@ .8936	"	"	1 78	
						126					
						150					
						176					
						200					
					5	Total					5 18
							SECOND GRADE				
						36			Per Box		
						48					
						64					
					1	80	@ $1.0054	"	"	1 00	
					1	100	@ .7318	"	"	73	
					1	126	@ .7318	"	"	73	
						150					
						176					
						200					
					3	Total					2 46
					8	Total Packed Boxes					
					19#	Standards Sold Loose @ $ .4750 Cwt.					9
						Culls Sold Loose					
						Culls Processed					
						Culls Worthless					
						Gross Returns					7 73

Statement of Account

	Debit	Credit
Gross Returns This Pool		7 73
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	58	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	72	
Growers Supplies Purchased		
Cash Advances		
Credit to Account		
Balance Due		
Check to Balance	6 43	
Total	7 73	7 73

Your pool average is $ 96 per packed box
In Addition there will be a Cash Refund estimated at $ 15 per packed box

Total Average $1 11 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—May 10 33
Pool No.—Three
From Jan 16 to Mar 15

Grower—J G Powell
Address—Redlnds

Variety—Navels

Record of Fruit Received					Credits							
Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size		FIRST GRADE			Amount	Totals
					2	80	@	$1.0641	Per	Box	2 13	
Jan 20	19960	8			18	100	@	1.1075	"	"	19 93	
Mar 1	20555	72			58	126	@	.8113	"	"	47 05	
	20556	72			70	150	@	.6905	"	"	48 33	
	20557	65			67	176	@	.6854	"	"	45 92	
2	20565	72			32	200	@	.5672	"	"	18 15	
	20566	72			29	216	@	.5519	"	"	16 00	
	20570	72			16	252	@	.5493	"	"	8 79	
	20572	72			4	288	@	.5251	"	"	2 10	
	20574	72			1	344	@	.5227	"	"	52	
	20579	22				392	@	.5287	"	"		
3	20584	72				Jumbles						
	20585	72										
	20587	72			297	Total						208 92
	20589	72						SECOND GRADE				
	20593	72				80	@	$ .3009	Per	Box		
	20597	69			5	100	@	.3490	"	"	1 74	
		1028			24	126	@	.3485	"	"	8 36	
[In pencil]:					43	150	@	.3371	"	"	14 49	
		61			48	176	@	.3372	"	"	16 18	
		15			48	200	@	.3389	"	"	16 26	
		16			40	216	@	.3386	"	"	13 54	
		73			27	252	@	.3321	"	"	8 96	
		—			16	288	@	.3260	"	"	5 21	
		3			6	344	@	.3070	"	"	1 84	
					2	392	@	.2350	"	"	47	
						Jumbles						
Note: Fruit Somewhat Coarse												
[In pencil]:					259	Total						87 05
262												
4 81					556	Total Packed Boxes						
9 09												
275 90	Debtor Ex 16				6381#	Standards Sold Loose @ $ .3339 Cwt.						21 30
					843#	Culls Sold Loose @ $ .2638 Cwt.						2 22
					852#	Culls Processed						
					120#	Culls Worthless						
						Gross Returns						319 49

Statement of Account

	Debit	Credit
Gross Returns This Pool		319 49
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	51 48	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	50 04	
Growers Supplies Purchased		
Fertilizer	57 00	
Smudge Oil	13 75	
G R Fellows Order	262 00	
Cash Advances		
Credit to Account		
Balance Due		114 78
Check to Balance		
Total	434 27	434 27

Your pool average is $ 57 per packed box
In Addition there will be a Cash Refund estimated at $ 20 per packed box

Total Average $ 77 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Oct 16 33

Grower—J G Powell
Address—Redlands

Pool No.—Two
From July 1 to Aug. 31

Variety—Valencias

Record of Fruit Received

Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	Credits FIRST GRADE			Amount	Totals
						80	Per Box				
						100					
July 26	21736	61				126					
					2	150	@ $1.3319	"	"	2 66	
					3	176	@ 1.3085	"	"	3 92	
					5	200	@ 1.1847	"	"	5 92	
					6	216	@ 1.0180	"	"	6 11	
					7	252	@ .9542	"	"	6 68	
					5	288	@ .7672	"	"	3 83	
					2	344	@ .6742	"	"	1 35	
						392	@ .6712	"	"		
						Jumbles					
					30	Total					30 47
							SECOND GRADE				
						80	Per Box				
						100					
						126					
						150					
					1	176	@ $ .5881	"	"	59	
					2	200	@ .5393	"	"	1 08	
					2	216	@ .6219	"	"	1 24	
					2	252	@ .4543	"	"	91	
					2	288	@ .4492	"	"	90	
					1	344	@ .2957	"	"	29	
						392	@ .2640	"	"		
						Jumbles					
					10	Total					5 01
					40	Total Packed Boxes					
					110#	Standards Sold Loose @ $ 5238 Cwt.					57
						Culls Sold Loose					
					40#	Culls Processed					
						Culls Worthless					
						Gross Returns					36 05

Statement of Account

	Debit	Credit
Gross Returns This Pool		36 05
Credit Balance Fdw.		
Debit Balance Fdw.	92 30	
Picking	3 35	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	3 60	
Growers Supplies Purchased		
Cash Advances		
Credit to Account		
Balance Due		63 20
Check to Balance		
Total	99 25	99 25

Your pool average is $ 90 per packed box
In Addition there will be a Cash Refund estimated at $ 20 per packed box

Total Average $1 10 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Oct 5 33

Grower—J G Powell
Address—Redlands

Pool No.—Two
From June 1 to June 30

Variety—Local Grapefruit

Record of Fruit Received

Date	Ticket No.	Field Boxes	√	Weight
June 8	21495	15		

Credits

Boxes	Size	FIRST GRADE	Amount	Totals
	36	Per Box		
	48			
1	64	@ $1.4900 " "	1 49	
1	80	@ 1.5100 " "	1 51	
1	100	@ 1.5100 " "	1 51	
1	126	@ 1.3500 " "	1 35	
	150			
	176			
	200			
4	Total			5 86
		SECOND GRADE		
	36	Per Box		
	48			
	64			
1	80	@ $ .9845 " "	98	
1	100	@ .9698 " "	97	
1	126	@ .9508 " "	95	
1	150	@ .7400 " "	74	
	176			
	200			
4	Total			3 64
8	Total Packed Boxes			
62#	Standards Sold Loose @ $.7561 Cwt.			47
	Culls Sold Loose			
	Culls Processed			
10#	Culls Worthless			
	Gross Returns			9 97

Statement of Account

	Debit	Credit
Gross Returns This Pool		
Credit Balance Fdw.		
Debit Balance Fdw.	100 88	
Picking	67	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	72	
Growers Supplies Purchased		
Cash Advances		
Credit to Account		
Balance Due		92 30
Check to Balance		
Total	102 27	102 27

Your pool average is $ per packed box

In Addition there will be a Cash Refund estimated at $ per packed box

Total Average $ per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Jun 20 33

Grower—J G Powell
Address—Redlands

Pool No.—Season Variety—Bloods
From..... To.....

Record of Fruit Received

Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	Credits FIRST GRADE	Amount	Totals
						80	Per Box		
						100			
						126			
Mar 8	20626	16				150			
						176			
						200			
						216			
Note: Fruit Quite Small Sized					1	252	@ $1.1753 " "	1 17	
					2	288	@ .9126 " "	1 82	
					4	344	@ .8122 " "	3 25	
						392			
						Jumbles			
					7	Total			6 24
							SECOND GRADE		
						80	Per Box		
						100			
						126			
						150			
						176			
						200			
						216			
						252			
						288			
						344			
						392			
						Jumbles			
						Total			
					7	Total Packed Boxes			
						Standards Sold Loose			
						Culls Sold Loose			
					270#	Culls Processed			
						Culls Worthless			
						Gross Returns			6 24

Statement of Account

	Debit	Credit
Gross Returns This Pool		6 24
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	80	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	63	
Growers Supplies Purchased		
Cash Advances		
Credit to Account	4 81	
Balance Due		
Check to Balance		
Total	6 24	6 24

Your pool average is $ 89 per packed box
In Addition there will be a Cash Refund estimated at $ 20 per packed box

Total Average $1 09 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Jun 20 33

Grower—J G Powell
Address—Redlands

Pool No.—Season Variety—Seeds
From..... To.....

Record of Fruit Received					Credits				
Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	FIRST GRADE	Amount	Totals
						80	Per Box		
Mar 31	21002	73				100			
						126			
					1	150	@ $ .4891 " "	49	
					2	176	@ .4945 " "	99	
					3	200	@ .4962 " "	1 49	
					4	216	@ .4963 " "	1 98	
					6	252	@ .4902 " "	2 94	
					9	288	@ .4583 " "	4 12	
					6	344	@ .3857 " "	2 31	
						392			
						Jumbles			
					31	Total			14 32
							SECOND GRADE		
						80	Per Box		
						100			
						126			
						150			
						176			
						200			
						216			
					1	252	@ $ .4367 " "	43	
					2	288	@ .4051 " "	81	
					1	344	@ .3285 " "	33	
						392			
						Jumbles			
					4	Total			1 57
					35	Total Packed Boxes			
						Standards Sold Loose			
						Culls Sold Loose			
					860#	Culls Processed			
						Culls Worthless			
						Gross Returns			15 89

Statement of Account

	Debit	Credit
Gross Returns This Pool		15 89
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	3 65	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	3 15	
Growers Supplies Purchased		
Cash Advances		
Credit to Account	9 09	
Balance Due		
Check to Balance		
Total	15 89	15 89

Your pool average is $ 45 per packed box
In Addition there will be a Cash Refund estimated at $ 20 per packed box

Total Average $ 65 per packed box

E. Fuller, President — Geo. T. Musson, Secretary

Redlands, California 11/17/34

REDLANDS HEIGHTS GROVES

Powell — Oranges Sunkist Lemons — Phone, Main 1324

OFF BLOOM NAVEL ORANGES

October 22 received 21 boxes.....	1047#	Door weight	
Less Cullage & Shrinkage	79#		
Sold Loose	968#	@ $2.3304 Cwt.	$22.56
Picking		$ 4.20	
		$ 4.20	$22.56
Credit to Account.....		18.36	
		$22.56	$22.56

[In pencil]:

Debtor Ex 15

43.96
11.32
55.75
3.41
5.05

119.49

[89]

nal Statement

Grower—
Address...

Record o
Date Ticket N

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Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Jun 15 34
Pool No.—Two
From Jan 16 to End of Season

Grower—J G Powell
Address.....

Variety—Navels

Record of Fruit Received

Date	Ticket No.	Field Boxes	√	Weight
Mar 1	23280	42		
	23281	64		
	23292	70		
2	23301	25		
	23309	72		
	23313	65		
		338		

Credits

Boxes	Size				Amount	Totals
		FIRST GRADE				
1	80	@	$ .6885	Per Box	69	
10	100	@	.5403	" "	5 40	
17	126	@	.6158	" "	10 47	
12	150	@	.7214	" "	8 66	
11	176	@	.8965	" "	9 86	
5	200	@	1.0717	" "	5 36	
4	216	@	1.0534	" "	4 21	
2	252	@	1.2103	" "	2 42	
1	288	@	1.2539	" "	1 25	
	344	@	1.2717	" "		
	392	@	1.2071	" "		
	Jumbles					
63	Total					48 32

Note: Fruit Inclined to be Large & Coarse

		SECOND GRADE				
	80	@	$1.3136	Per Box		
	100	@	.3496	" "		
30	126	@	.3826	" "	11 48	
16	150	@	.4831	" "	7 73	
13	176	@	.6796	" "	8 83	
9	200	@	.7310	" "	6 58	
5	216	@	.8561	" "	4 28	
2	252	@	.9559	" "	1 91	
1	288	@	1.0102	" "	1 01	
	344	@	1.0322	" "		
	392	@	1.0322	" "		
	Jumbles					
76	Total					41 82
139	Total Packed Boxes					
5280#	Standards Sold Loose @ $ .7096 Cwt.					37 47
	Culls Sold Loose					
700#	Culls Processed					
120#	Culls Worthless					
	Gross Returns					127 61

Statement of Account

	Debit	Credit
Gross Returns This Pool		127 61
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	18 26	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	12 51	
Growers Supplies Purchased		
Fertilizer	52 88	
Cash Advances		
Credit to Account	43 96	
Balance Due		
Check to Balance		
Total	127 61	127 61

Your pool average is $ .92 per packed box
In Addition there will be a Cash Refund estimated at $ .20 per packed box

Total Average $1.12 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Oct 27 1934
Pool No.—One Variety—Valencias
From Beginning of Season to End of Season

Grower—J G Powell
Address.....

Record of Fruit Received

Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	Credits FIRST GRADE		Amount	Totals
						80	Per Box			
						100	@ $1.8122	" "		
July 18	520	13				126	1.9638			
						150	1.9891			
						176	2.0513			
					1	200	2.0543		2 05	
					1	216	2.0490		2 05	
					1	252	2.0305		2 03	
					1	288	1.9713		1 97	
					1	344	1.5068		1 51	
						392	1.3447			
						Jumbles				
					5	Total				9 61
							SECOND GRADE			
						80	Per Box			
						100	@ $ .8915			
						126	1.2149			
						150	1.3666			
						176	1.6324			
						200	1.6257			
						216	1.5686			
					1	252	1.4391		1 44	
					1	288	1.2833		1 28	
						344	1.1865			
						392	1.0280			
						Jumbles				
					2	Total				2 72
					7	Total Packed Boxes				
					55#	Standards Sold Loose @ $1.0660 Cwt.				59
						Culls Sold Loose				
					40#	Culls Processed				
						Culls Worthless				
						Gross Returns				12 92

Statement of Account

	Debit	Credit
Gross Returns This Pool		12 92
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	97	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	63	
Growers Supplies Purchased		
Cash Advances		
Credit to Account	11 32	
Balance Due		
Check to Balance		
Total	12 92	12 92

Your pool average is $1 85 per packed box
In Addition there will be a Cash Refund estimated at $ 20 per packed box

Total Average $2 05 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Jun 27 34

Grower—J G Powell
Address.....

Pool No.—Season
From..... to.....

Variety—Seeds

Date	Record of Fruit Received Ticket No.	Field Boxes	√	Weight	Boxes	Size	Credits FIRST GRADE	Amount	Totals
						80	Per Box		
						100			
Mar 20	23499	72				126			
	23509	65				150			
	23510	10			1	176	@ $ .7618 " "	76	
					4	200	@ .7829 " "	3 13	
		147			9	216	@ .8875 " "	7 99	
					12	252	@ 1.0814 " "	12 98	
					13	288	@ 1.1104 " "	14 44	
					11	344	@ 1.0768 " "	11 84	
					5	392	@ .9946 " "	4 97	
						Jumbles			
					55	Total			56 11
							SECOND GRADE		
						80	Per Box		
						100			
						126			
					1	150	@ $ .2652 " "	27	
					2	176	@ .4675 " "	94	
					4	200	@ .6418 " "	2 57	
					5	216	@ .7667 " "	3 83	
					5	252	@ .7751 " "	3 88	
					5	288	@ .7911 " "	3 96	
					3	344	@ .7692 " "	2 31	
					2	392	@ .5120 " "	1 02	
						Jumbles			
					27	Total			18 78
					82	Total Packed Boxes			
						Standards Sold Loose			
						Culls Sold Loose			
					740#	Culls Processed			
					60#	Culls Worthless			
						Gross Returns			74 89

Statement of Account

	Debit	Credit
Gross Returns This Pool		74 89
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	11 76	
Hauling		
Building and Supply Co. Revolving Stock		
@ 9c per packed box	7 38	
Growers Supplies Purchased		
Cash Advances		
Credit to Account	55 75	
Balance Due		
Check to Balance		
Total	74 89	74 89

Your pool average is $ 91 per packed box
In Addition there will be a Cash Refund estimated at $ 20 per packed box

Total Average $1 11 per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Jul 2 34

Grower—J G Powell
Address.....

Pool No.—Season
From..... To.....

Variety—Bloods

Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	Credits FIRST GRADE	Amount	Totals
						80	Per Box		
Mar 20	23511	11				100			
						126			
						150			
						176			
						200			
						216			
						252			
					1	288	@ $1.1440 " "	1 14	
					1	344	@ 1.1086 " "	1 11	
					1	392	@ 1.0264 " "	1 03	
						Jumbles			
					1	420	@ .9346 " "	93	
					4	Total			4 21
							SECOND GRADE		
						80	Per Box		
						100			
						126			
						150			
						176			
						200			
						216			
						252			
						288			
						344			
						392			
						Jumbles			
					1	420	@ $ .5321 " "	53	
					1	Total			
					5	Total Packed Boxes			53
						Standards Sold Loose			
						Culls Sold Loose			
					140#	Culls Processed			
						Culls Worthless			
						Gross Returns			4 74

Statement of Account

	Debit	Credit
Gross Returns This Pool		4 74
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	88	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	45	
Growers Supplies Purchased		
Cash Advances		
Credit to Account	3 41	
Balance Due		
Check to Balance		
Total	4 74	4 74

Your pool average is $ per packed box

In Addition there will be a Cash Refund estimated at $ per packed box

Total Average $ per packed box

Final Statement

REDLANDS HEIGHTS GROVES, INC.

Redlands, Calif.—Oct 12 34

Grower—J G Powell
Address.....

Pool No.—One Variety—Grapefruit
From—Beginning of Season To End of Season

Record of Fruit Received					Credits				
Date	Ticket No.	Field Boxes	√	Weight	Boxes	Size	FIRST GRADE	Amount	Totals
July 18	521	7				36	Per Box		
						48			
					1	64	@ $1.4542 " "	1 45	
					1	80	@ 1.7837 " "	1 78	
					1	100	@ 1.5775 " "	1 58	
						126			
						150			
						176			
						200			
					3	Total			4 81
							SECOND GRADE		
						36	Per Box		
						48			
						64			
						80			
						100			
					1	126	@ $ .6945 " "	69	
						150			
						176			
						200			
					1	Total			69
					4	Total Packed Boxes			
					66#	Standards Sold Loose @ $.5002 Cwt.			33
						Culls Sold Loose			
						Culls Processed			
						Culls Worthless			
						Gross Returns			5 83

Statement of Account

	Debit	Credit
Gross Returns This Pool		5 83
Credit Balance Fdw.		
Debit Balance Fdw.		
Picking	42	
Hauling		
Building and Supply Co. Revolving Stock @ 9c per packed box	36	
Growers Supplies Purchased		
Cash Advances		
Credit to Account	5 05	
Balance Due		
Check to Balance		
Total	5 83	5 83

Your pool average is $1 46 per packed box
In Addition there will be a Cash Refund estimated at $ 20 per packed box

Total Average $1 66 per packed box

Joseph Harris, President Phone 2188 Geo. T. Musson, Secretary and Manager

REDLANDS HEIGHTS GROVES

Packers and Shippers Sunkist Oranges and Grapefruit

Redlands, California
1/29/43

[Written across face of page]: Dbtors Ex 1 for Identification Admitted

Schedule of Fruit Harvested by J. G. Powell From Home, or Clark Grove, and Wumkes Grove

	Home or Clark Grove			Wumkes grove		
1935–36	Navels	906 boxes	$629.11			
	Odds	201 "	129.50			
	Vals	58 "	60.19			
	refund		62.55			
	Total	1165 "	$878.35			
1936–37	Navels	880 bxs	$707.39			
	Odds	106 "	120.92			
	Vals.	56 "	62.68	Vals	872 bxs	$1543.88
	Refund		39.27	Refund		34.27
	Total	1042 "	930.26	Total	872 "	$1578.15
1937–38	Navels	702 bxs	$187.45	Navels	258 bxs	$ 77.27
	Odds	141 "	27.12			
				Vals	733 "	256.78
	Refund		45.37	Refund		53.34
	Total	843 "	$259.94	Total	991 "	$387.39
1938–39	Navels	893 bxs	$230.75	Navels	551 bxs	$150.08
	Odds	184 "	13.97			
	Vals.	59 "	24.79	Vals	1407 "	555.16
	Refund		34.51	Refund		59.48
	Total	1136 "	304.02	Total	1958 "	$764.72
1939–40	Navels	747 bxs	$344.07	Navels	455 bxs	$227.10
	Odds	225 "	151.18			
	Vals	29 "	14.68	Vals.	1528 "	934.94
	Refund		48.25	Refund		99.12
	Total	1001 "	$558.18	Total	1983 "	$1261.16
1940–41	Navels	1012 bxs	$496.53	Navels	723 bxs	$397.43
	Odds	145 "	58.22	Odds	16	19.65
	Vals	30 "	25.55	Vals	877	842.28
	Refund		37.02	Refund		47.51
	Total	1187 "	$617.32	Total	1616	$1306.87
						[100]
1941–42	Navels	1583 bxs	$705.67	Navels	878 bxs	$397.93
	Odds	177 "	72.76	Odds	27 "	16.08
	Vals.	67 "	95.09	Vals.	2156 "	2724.03
	Refund		101.11	Refund		149.02
		1827 "	$974.63	Total	3061 "	$3287.06
2–10–43	Navels	416 bxs		Nvels	263 Bxs	
Estimated now on trees:						
	Vals.	10 Bxs		Vls.	300 Bxs	
	Odds	60 Bxs		Ods	5 Bxs	

[101]

[Title of District Court and Cause.]

NOTICE OF HEARING

Notice Is Hereby Given that Petition for reappraisal or Hearing to determine value of real property of above named debtors, has been filed in this court.

Your Are Further Notified, that Hearing on said Petition, will be held at the office of the undersigned Conciliation Commissioner-Referee, 318 Katz Bldg., San Bernardino, California, on Wednesday, the 3rd., day of March, 1943, at the hour of Ten o'clock A. M., of said day, when all parties interested may appear and present their evidence in the manner provided by Law.

Dated, February, 16th., 1943.

FRED DUFFY

Conciliation Commissioner-Referee for San Bernardino County, California.

I hereby certify that on Feby. 16th 1943 I mailed to all parties in interest copy of above named notice of hearing. That the notice mailed to Peter J. Wumkes a secured creditor was addressed to 10800 Lindbrook Ave West Wood Village

FRED DUFFY

Concil. Comm.-Referee [102]

To the Creditors of James Goodwin Powell and Anna Strachan Powell, of Redlands, San Bernardino County, and District and State Aforesaid, Bankrupts:

Notice Is Hereby Given that a Petition Requesting Court Re-appraisal or Hearing to Determine Value of Debtors' Real Property has been duly and regularly filed and that the Honorable Fred Duffy, Conciliation Commissioner, has set said matter for hearing on Tuesday, February 2, 1943, at the hour of ten o'clock A. M., said hearing to be held in the office of the said Fred Duffy, Conciliation Commissioner, 318 Katz Building, San Bernardino, California, at which time the said creditors, or anyone interested, may attend and be heard.

FRED DUFFY
Referee in Bankruptcy under Section 75(s) of the Bankruptcy Act, San Bernardino County, California, and Conciliation Commissioner.

[Endorsed]: Filed 1/20/43. Fred Duffy, Council Comm. [103]

[Title of District Court and Cause.]

PETITION REQUESTING COURT RE-APPRAISAL OR HEARING TO DETERMINE VALUE OF DEBTORS' REAL PROPERTY

To the Honorable Fred Duffy, Conciliation Commissioner of the Above Entitled Court for the County of San Bernardino, State of California.

Your Petitioner, James Goodwin Powell and Anna Strachan Powell, Debtors in the above entitled proceedings, respectfully represents to this Honorable Court as follows, to-wit:

I.

That on or about the 25th day of July 25, 1940, your petitioners filed their joint petition in the above entitled Court praying for relief as provided for in the provisions of Section 75 of the Bankruptcy Act; that the filing of said petition was approved by the above entitled Court and referred to Fred Duffy, Esq., Conciliation Commissioner, for further proceedings.

II.

That on or about the 24th day of October, 1940, your petitioners having been unable to secure acceptance or confirmation of their ext*n*sion proposal, filed their amended petition and [104] were adjudicated bankrupts in accordance with the provisions of Section 75(s) of the Bankruptcy Act; and that the above entitled matter was referred to

the Honorable Fred Duffy, Conciliation Commissioner, for further proceedings; that thereafter on the 16th day of June, 1941, said Honorable Fred Duffy, Conciliation Commissioner, made and entered an order setting aside exempt properties to debtors, giving debtors possession of their properties for a period of three years, and setting the rental to be paid by the debtors.

III.

That scheduled by debtors in their schedules was the following described real property owned by debtors and situated in the County of San Bernardino, State of California, more particularly described as follows, to-wit:

Parcel 1: That property in the City of Redlands, County of San Bernardino, State of California, described as:

That portion of the Northwest quarter of the Southeast quarter of Section 21, Township 1 South, Range 3 West, San Bernardino Base & Meridian, described as: Beginning on the north line of said northwest quarter of Southeast quarter 1008.87 feet East of the Northwest corner of said southeast quarter; thence south along the east line of land of Israel Beal, 853.33 feet to a point 466.67 feet north of the south line of said northwest quarter of the southeast quarter; thence west 342 feet; thence north and parallel with first course herein, 853.33 feet; thence East 342 feet to beginning; Except that portion conveyed to the Lugo Water Com-

pany by deed recorded in Book 438 of Deeds, at page 384 described as follows: Commencing at the northeast corner of the southeast ¼ of said section; thence West along the center line of Lugonia Avenue, 1716 feet for point of beginning; thence South 0 degrees 12′ East 48 feet; thence West 55 feet; thence north 0 degrees 12′ West 48 feet; thence east 55 feet to the place of beginning. Together with Four (4) shares of the capital stock of the Lugo Water Company, a corporation.

Parcel 2: That property in the City of Redlands, County of San Bernardino, State of California, described as:

All that portion of the northwest quarter of the southeast quarter of Section 21, Township 1 South Range 3 West, San Bernardino Base & Meridian, in the City of Redlands, according to Government Survey, [105] described as follows:

Beginning at a point on the east boundary line of the above described tract, which is 718.07 feet north from the southeast corner thereof; thence running north along the east boundary line thereof 597.08 feet, more or less, to the northeast corner of said tract; thence west along the north boundary line thereof, 311.13 feet, more or less, to a point which is 1,008.87 feet east from the northwest corner of said tract; thence southerly on a line parallel with the east boundary of said tract 597.08

feet, more or less, to a point due west of the point of beginning; thence east 311.13 feet, more or less, to the beginning. Together with 5 shares of the capital stock of the Lugonia Water Company, a corporation.

IV.

That your petitioners are desirous of having this Court appoint appraisers to reappraise the above described real property or, in the alternative, in the discretion of this Court, to call a meeting or hearing to determine the value of your petitioners' real property.

Wherefore, your petitioners pray and request that this Court appoint appraisers to reappraise the debtors' real property under the provisions of subsection (3) of Section 75(s) of the Bankruptcy Act and/or, in the discretion of this Court, that the Court set a time and place for a hearing in the above entitled proceedings to determine the value of the debtors' real property.

Respectfully submitted.

JAMES GOODWIN POWELL
Debtor

H. R. GRIFFIN
Attorney for Debtor

[Endorsed]: Filed 12/23/42. Fred Duffy, Council Comm. [106]

State of California,
County of San Bernardino—ss

James Goodwin Powell being by me first duly sworn, deposes and says: That he is one of the Petitioners in the above entitled action; that he has read the foregoing Petition and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon his information or belief, and as to those matters that he believes it to be true.

JAMES GOODWIN POWELL

Subscribed and sworn to before me this 23rd day of December, 1942

H. R. GRIFFIN
Notary Public in and for Said
(Seal) County and State

[Endorsed]: Filed July 19, 1943. Edmund L Smith, Clerk, by E. M. Enstrom, Deputy. [107]

[Title of District Court and Cause.]

NOTICE OF HEARING PETITIONS TO REVIEW

To James Goodwin Powell and Anna Strachan Powell, the Debtors Above Named, and to H. R. Griffin, Esq., Attorney at Law:

You, and each of you, will please take notice that on Tuesday, August 10, 1943, at the hour of 10:00 o'clock, A. M., before the Hon. Leon R. Yankwich, Judge of the United States District Court, in the

Federal Building, Los Angeles, California, the petitions to review those certain orders of May 18, 1943, and April 9, 1943, made and entered in these proceedings by the Hon. Fred Duffy, Conciliation Commissioner for the County of San Bernardino, will be heard.

Dated this 30th day of July, 1943.

NICHOLS, COOPER & HICKSON
Attorneys for Petitioner
By (ILLEGIBLE)
Of Counsel [108]

[Title of District Court and Cause.]

AFFIDAVIT OF MAILING

State of California
County of Los Angeles—ss

Jean Sinness, on oath, says: I am a citizen of the United States, and a resident of said County. I am over the age of eighteen years and not a party to the above-entitled action. My business address is 650 South Spring Street, Los Angeles, California. On the 31st day of July, 1943, I served the attached Notice of Hearing Petitions to Review on the above-named debtors and on H. R. Griffin, Esq., Attorney at Law, by putting a true copy thereof enclosed in each of three sealed envelopes addressed as follows: one to James Goodwin Powell, c/o H. R. Griffin, Esq., Attorney at Law, Katz

Building, San Bernardino, California; one to Anna Strachan Powell, c/o H. R. Griffin, Esq., Attorney at Law, Katz Building, San Bernardino, California; and one to H. R. Griffin, Esq., Attorney at Law, Katz Building, San Bernardino, California, in the postoffice at Los Angeles, California, with postage thereon fully prepaid. There is regular communication by mail between the place of mailing and the place so addressed.

JEAN SINNESS

Subscribed and sworn to before me this 31st day of July, 1943.

CLARA KLEINMAN
Notary Public in and for said County and State.

[Endorsed]: Filed Aug. 2, 1943. [109]

[Title of District Court and Cause.]

AFFIDAVIT RE APPRAISAL OF PROPERTY OF LOUIS A. TURNER.

State of California
County of Los Angeles—ss.

Louis A. Turner, being first duly sworn, deposes and says:

That he is engaged in the business of growing, packing and shipping citrus fruit; that he has engaged in said business since 1925; that he is familiar with the properties in the Redlands citrus district and particularly with the orange grove owned by

James Goodwin Powell and Anna Strachan Powell upon which Peter J. Wumkes has a lien; that your affiant has gone over said properties on several occasions during the past six months; that said property consists of approximately 6½ acres and is planted with approximately 800 trees, 3/4ths to valencias and 2/5ths to navels; that your affiant has made thousands of appraisals of properties; that he has made all of the appraisals for James A. Burrell and Hale P. Powers both of whom have bought and sold hundreds of acres of citrus property upon the appraisals made by your affiant; that your affiant is familiar with the value of the Powell property since March 1st, 1943 and fixes the value thereof at $8,500.00.

L. A. TURNER

Subscribed and Sworn to before me this 17th day of September, 1943.

ETHYL BALDWIN

Notary Public in and for said

(Seal) County and State. [111]

Received copy of the within affi. this 20th day of Sept., 1943.

H. R. GRIFFIN

[Endorsed]: Filed Sept. 20, 1942. [112]

[Title of District Court and Cause.]

AFFIDAVIT RE APPRAISAL OF PROPERTY OF K. C. O'BRYAN [113]

State of California,
County of Los Angeles,—ss.

K. C. O'Bryan, being first duly sworn, deposes and says: That he is the President of Southern Citrus Association, a corporation engaged in the growing, packing and shipping of citrus fruits; that he has lived in the Redlands citrus district for the past seventeen years; that in connection with the operation of his business he has made hundreds of inspections and appraisals of citrus properties in this location; that he is familiar with the orange grove owned by James Goodwin Powell and Anna Strachan Powell upon which Peter J. Wumkes holds a note secured by Deed of Trust and during several seasons handled the fruit from said property; that said property consists of approximately six and seven tenths acres and is planted with 798 trees, of which 494 are valencias and 304 navels. That affiant owns several citrus properties in the vicinity of the Powell grove; that he has on numerous recent occasions gone over the Powell property; that he is familiar with the value of said property as it existed during the year 1943; that based on said experience, this affiant fixes the reasonable value of said property on March 4th, 1943 and at the present time, at the sum of $8,000.00; that your affiant is familiar with the terms of sale

of an orange grove across the street from the Powell grove, which was sold shortly after the month of March, 1943, for a price in excess of $1,100.00 per acre, which property was considered of the [114] same general class as the Powell property and that other groves in the immediate vicinity of the Powell grove have sold recently for as high as $2,000.00 per acre.

That in appraising said property, your affiant, if permitted to purchase said property, would be willing to pay the sum of $6,500.00 cash and herewith makes such an offer.

K. C. O'BRYAN

Subscribed and Sworn to before me this 16th day of September, 1943.

ETHYL BALDWIN
Notary Public in and for
County of Los Angeles,
(Seal) State of California. [115]

Received copy of the within this 20th day of Sept., 1943.

H. R. GRIFFIN

[Endorsed]: Filed Sept. 20, 1943. [116]

[Title of District Court and Cause.]

AFFIDAVIT OF CREDITOR

State of California,
County of Los Angeles,—ss.

Peter J. Wumkes, being first duly sworn, deposes and says: That he is a creditor of the above-named debtors, James Goodwin Powell and Anna Strachan Powell; that said indebtedness arises by reason of Trust Deeds taken upon property sold to said debtors during the year 1938; that the total sale price of said property at said time was $13,500.00, of which $2,500.00 was paid in cash the balance being secured by Trust Deeds against said property; that since said time said debtors have paid absolutely nothing on account of said Trust Deeds, nor has said creditor received notice of any funds being deposited for his account by said debtors. That since said debtors filed their petition in bankruptcy, your affiant has received nothing whatsoever and neither has he received any payments whatsoever on account of rent order made by the Conciliation Commissioner on the 16th day of June, 1941, by which order one-fourth of the proceeds of the crop were fixed as rental to be paid each year starting June 1st, 1942. [117]

That your affiant further believes and upon such information and belief alleges the fact to be that there is due and a lien against the property of said debtors, upon which your affiant has a lien, a sum in excess of Two Hundred Dollars due the County of San Bernardino and the City of Redlands for delinquent taxes for the years 1938 and 1939.

That your affiant owned the property in question for approximately two years prior to the sale to the above-named debtors and since the sale to said debtors has on numerous occasions, inspected said property and is familiar with the condition thereof and is familiar with values of property in the immediate vicinity of debtors' property, as well as with the value of debtors' property. That your affiant alleges the value of said property of said debtors to be the sum of $10,000.00

PETER J. WUMKES
Creditor

Subscribed and Sworn to before me this 17th day of September, 1943.

ETHYL BALDWIN
Notary Public in and for above County and State.
(Seal) [118]

Received copy of the within aff. this 20th day of Sept., 1943.

H. R. GRIFFIN

[Endorsed]: Filed Sept. 20, 1943. [119]

AFFIDAVIT OF DONALD P. NICHOLS

State of California,
County of Los Angeles,—ss.

Donald P. Nichols, being first duly sworn, deposes and says: That he is a member of the firm of Nichols, Cooper & Hickson, attorneys for Peter J. Wumkes in the matter of the bankruptcy of

James Goodwin Powell and Anna S. Powell; that on the hearing of the petition for re-determination of appraised value of property of the bankrupts, your affiant presented to the Conciliation Commissioner an offer, in writing, upon the property against which Mr. Wumkes holds a lien, in the sum of $5500.00 and attached thereto a check in the amount of $550.00; that said cash offer was made by Orange Belt Fruit Distributors. That the Conciliation Commissioner refused to receive said offer and refused to permit your affiant, as counsel, to file said offer with said Conciliation Commissioner. That after the petition for review was filed, your affiant, on several occasions, requested of the Conciliation Commissioner, a statement or accounting as to disbursement of funds which had been received by the Conciliation Commissioner. That the said Conciliation Commissioner has at all times refused to furnish either your affiant or the said Peter J. Wumkes, creditor, with any statement of accounting whatsoever, and has refused to furnish affiant with a statement showing that no monies whatsoever have been paid to said Peter J. Wumkes on account of the rent order which was made in said proceedings. [120]

DONALD P. NICHOLS

Subscribed and Sworn to before me this 20th day of September, 1943.

(Seal) ETHYL BALDWIN

Notary Public in and for above County and State.

[Endorsed]: Filed Sept. 20, 1943. [121]

OFFER TO PURCHASE

The undersigned, hereby offers to purchase the property hereinafter described, being known as the James Goodwin Powell property upon which P. J. Wumkes holds a Trust Deed and does hereby offer to purchase said property for the sum of $7,000.00 and does hereby tender cashier's check of $700.00 being ten per cent (10%) of the amount of said offer, the balance to be paid in cash at the time title to said property can be conveyed to the undersigned free and clear of encumbrances except reservations and restrictions of record.

The property on which the offer of purchase is made is described as follows:

That property in the City of Redlands, County of San Bernardino, State of California, described as:

That portion of the Northwest quarter of the Southeast quarter of Section 21, Township 1 South, Range 3 West, San Bernardino Base & Meridian, described as: Beginning on the North line of said northwest quarter [122] of Southeast quarter 1008.87 feet East of the Northwest corner of said Southeast quarter; thence South along the East line of land of Israel Beal, 853.33 feet to a point 466.67 feet North of the South line of said Northwest quarter of the Southeast quarter; thence West 342 feet; thence North and parallel with first course herein, 853.33 feet; thence East 342 feet to beginning;

Except that portion conveyed to the Lugo

Water Company by Deed recorded in Book 438 of Deeds, at page 384 described as follows:

Commencing at the Northeast corner of the Southeast ¼ of said section; thence West along the center line of Lugonia Avenue, 1716 feet for point of beginning; thence South 0 degrees 12′ East 48 feet; thence West 55 feet; thence North 0 degrees 12′ West 48 feet; thence East 55 feet to the place of beginning.

Together With Four (4) shares of the capital stock of the Lugo Water Company, a corporation.

Dated this 17th day of September, 1943.

JOHN CURCI

[Endorsed]: Filed Sept. 20, 1943. [123]

In the District Court of the United States
Southern District of California
Central Division

No. 36775-C

In the Matter of

JAMES GOODWIN POWELL and ANNA STRACHAN POWELL, husband and wife,

Debtors.

Book 21 Page 210

ORDER

The Petition on Review of Peter J. Wumkes from those two orders of the Conciliation Commissioner

of San Bernardino County dated April 9th, 1943 and May 18th, 1943, respectively, coming on to be heard the 20th day of September, 1943 before the Honorable Leon R. Yankwich, Judge of the above entitled Court, the petitioner appearing in person and by his counsel Messrs. Nichols, Cooper & Hickson, by Donald P. Nichols and C. P. Von Herzen, Esquires, and the debtors appearing by their counsel, H. R. Griffin, Esq., and the Court having considered the certificates on review, the evidence and the proofs submitted, and having heard the argument of counsel with respect thereto, and being fully advised in the premises, now makes its order as follows:

It Is Ordered and Adjudged that the order of the Conciliation Commissioner of San Bernardino County dated April 9th, 1943, be and the same is hereby reversed; [124]

It Is Further Ordered and Adjudged that the order of the Conciliation Commissioner of San Bernardino County dated May 18th, 1943, be and the same is hereby reversed;

It Is Further Ordered and Adjudged that this matter be referred to the Conciliation Commissioner of San Bernardino County for a further hearing on the matter of the value of the real property in controversy, and that upon such further hearing, or prior thereto, the petitioner herein, Peter J. Wumkes, pay to the attorney for the debtors, the sum of Fifty Dollars ($50.00) as a condition precedent to such further hearing.

Dated: September 30, 1943.

LEON R. YANKWICH
United States District Court
Judge

Judgment entered Oct. 1, 1943. Docketed Oct. 1, 1943. Book 21, Page 210.

EDMUND L. SMITH,
Clerk,
By LOUIS J. SOMERS
Deputy.

Approved as to form:

C. P. VON HERZEN
For Nichols, Cooper & Hickson
H. R. GRIFFIN
Attorney for Debtors

[Endorsed]: Filed Sept. 30, 1943. [125]

[Title of District Court and Cause.]

NOTICE OF APPEAL

To the United States Circuit Court of Appeals for the Ninth Circuit Court for Rule 73(b).

Notice Is Hereby Given That, James Goodwin Powell and Anna Strachan Powell, husband and wife, debtors in the above bankruptcy proceeding, hereby appeal to the United States Circuit Court of Appeals for the Ninth Circuit, from the order and judgment of the Honorable Leon R. Yankwich,

Judge of the United States District Court, made, entered and filed in the records of the above said Court on the 30th day of September, 1943, reversing the order of the Conciliation Commissioner of San Bernardino County made and dated April 9, 1943, and further reversing the order of the Conciliation Commissioner of San Bernardino County dated May 18, 1943, and further ordering that said matter be referred to the Conciliation Commissioner of San Bernardino County for a further hearing on the matter of the value of the real property in controversy, and that upon such further hearing, or prior thereto, the petitioner therein, Peter J. Wumkes, pay to the attorney for the debtors the sum of Fifty ($50.00) Dollars as a condition precedent to such further hearing, and from each of them.

Dated this 26th day of October, 1943.

H. R. GRIFFIN

Attorney for Debtors and Appellants. [126]

Notice is further given that the parties interested in this appeal are Peter J. Wumkes represented by Messrs. Nichols, Cooper and Hixon, 412-418 First National Building, Pomona, California, and C. P. Von Herzen, 453 South Spring Street, Los Angeles, Attorneys at Law.

Copies mailed 10/29/43

TH

[Endorsed]: Filed Oct. 27, 1943. [127]

[Title of District Court and Cause.]

UNDERTAKING FOR COSTS ON APPEAL

Know All Men By These Presents, that the Fidelity and Deposit Company of Maryland, a corporation organized and existing under the laws of the State of Maryland, and duly licensed to transact business in the State of California, is held and firmly bound unto Peter J. Wumkes, in the penal sum of Two Hundred Fifty and No/100—Dollars ($250.00), to be paid to the said Peter J. Wumkes, his successors or assigns, or legal representatives, for which payment well and truly to be made, the Fidelity and Deposit Company of Maryland binds itself, its successors and assigns, firmly by these presents.

The Condition of the Above Obligation Is Such that

Whereas, James Goodwin Powell and Anna Strachan Powell, husband and wife, have appealed, or are about to appeal to the United States Circuit Court of Appeals for the Ninth Circuit, from an Order and Judgment of the Honorable Leon R. Yankwich, Judge of the United States District Court, made, entered and filed in the records of the above said Court on the 30th day of September, 1943, reversing the Order of the Conciliation Commissioner of San Bernardino County made and dated April 9, 1943, and further reversing the Order of the Conciliation Commissioner of San Bernardino County dated May 18, 1943, in the above entitled action. [128]

Now, Therefore, if the above named Appellants, James Goodwin Powell and Anna Strachan Powell, husband and wife, shall prosecute said appeal to effect and answer all costs which may be adjudged against them if the appeal is dismissed, or the Order affirmed, or such costs as the Appellate Court may award if the Order is modified, or in any other event, then this obligation shall be void; otherwise to remain in full force and effect.

It Is Hereby Agreed by the Surety that in case of default or contumacy on the part of the Principals or Surety, the Court may, upon notice to them of not less than ten days, proceed summarily and render judgment against them, or either of them, in accordance with their obligation, and award execution thereon.

Signed, sealed and dated this 27th day of October, 1943.

FIDELITY AND DEPOSIT
COMPANY OF MARYLAND
By W. M. WALKER
Attorney in Fact
Attest S. M. SMITH
Agent

Examined and recommended for approval as provided in Rule 13.

H. R. GRIFFIN
Attorney

State of California,
County of Los Angeles,—ss:

On this 27th day of October, 1943, before me, Theresa Fitzgibbons, a Notary Public, in and for the said County of Los Angeles, State of California, residing therein, duly commissioned and sworn, personally appeared W. M. Walker, known to me to be the Attorney-in-Fact, and S. M. Smith, known to me to be the Agent of the Fidelity and Deposit Company of Maryland, the Corporation that executed the within instrument, and acknowledged to me that they subscribed the name of the Fidelity and Deposit Company of Maryland thereto and their own names as Attorney-in-Fact and Agent, respectively.

THERESA FITZGIBBONS
Notary Public in and for the County of Los Angeles, State of California.
My Commission Expires May 3, 1946.

[Endorsed]: Filed Oct. 27, 1943. [129]

[Title of District Court and Cause.]

DESIGNATION OF PORTIONS OF RECORD TO BE CONTAINED IN RECORD ON APPEAL

To the Above Honorable Court and to the Clerk Thereof:

Notice Is Hereby Given that James Goodwin Powell and Anna Strachan Powell, husband and

wife, debtors and appellants, do hereby designate that the complete record and all of the proceedings and evidence in the above entitled matter are to be contained in the Record on Appeal.

Dated this 2nd day of November, 1943.

H. R. GRIFFIN

Attorney for Debtors and Appellants [130]

[Title of District Court and Cause.]

AFFIDAVIT OF MAILING

State of California
County of San Bernardino—ss.

Beatrice Oie, being first duly sworn, deposes and says: That her business address is 408 Katz Building, San Bernardino, California; that she is a citizen of the United States, and a resident of the County of San Bernardino; that she is over the age of eighteen years, and not a party to the above-entitled cause; that on the 2nd day of November, 1943, she placed a copy of the Designation of Portions of Record to Be Contained in Record on Appeal herein in an envelope addressed to the following persons and at the following address: Nichols, Cooper and Hickson, 412-18 First National Building, Pomona, California, sealed said envelope and deposited it in the U. S. mail at San Bernardino, California, with the postage thereon fully prepaid; that there is a regular communication by mail between the place of mailing and the place so addressed.

BEATRICE OIE

Subscribed and sworn to before me this 2nd day of November, 1943.

H. R. GRIFFIN

Notary Public in and for said County and State.

[Endorsed]: Filed Nov. 3, 1943. [131]

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 131 inclusive contain full, true and correct copies of: Debtor's Petition and Schedules; Approval of Debtor's Petition and Order of Reference; Amended Petition; Certificate of Conciliation Commissioner; Adjudication, Order of Reference and Temporary Restraining Order; Certificate on Review of Conciliation Commissioner's Order Dated May 18, 1943; Petition to Review Order of the Conciliation Commissioner under Date of May 18, 1943; Envelopes; Orders Extending Time for Filing Petition for Review; Notice of Order Denying Petition for Rehearing to Determine Value of Real Property; Order Denying Petition for Rehearing to Determine Value of Real Property; Notice of Hearing; Petition for Rehearing to Determine Value of Real Property; Certificate on Review of Conciliation Commissioner's Order of April 9, 1943 Finding Value of Real Property; En-

velope; Petition to Review Order of The Conciliation Commissioner under Date of April 9, 1943; Order Extending Time for Filing Petition for Review; Certificate Extending Time for Filing Petition for Review; Petition for Certificate Extending Time for Filing Petition for Review; Letter Dated May 11, 1943; Petition for Review of Order of Conciliation Commissioner; Notice of Entry of Order Determining Value of Debtors' Real Property; Order Determining Value of Debtors' Real Property; Findings of Fact and Conclusions of Law; Decision; Exhibits 1, 4, 8, 9, 10, 11, 12, 15, 16 and 17; Notice of Hearing; Notice; Petition Requesting Court Re-Appraisal or Hearing to Determine Value of Debtors' Real Property; Notice of Hearing Petitions to Review; Affidavit of Louis A. Turner; Affidavit of K. C. O'Bryan; Affidavit of Peter J. Wumkes; Affidavit of Donald P. Nichols; Offer to Purchase; Order; Notice of Appeal; Undertaking for Costs on Appeal and Designation of Portions of Record to be Contained in Record on Appeal which constitute the record on appeal to the Circuit Court of Appeals for the Ninth Circuit.

I further certify that my fees for comparing, correcting and certifying the foregoing record amount to $48.45 which sum has been paid to me by Appellants.

Witness my hand and the seal of said District Court this 11th day of November, 1943.

[Seal] EDMUND L. SMITH,
Clerk.
By THEODORE HOCKE
Deputy Clerk.

[Endorsed]: No. 10610. United States Circuit Court of Appeals for the Ninth Circuit. James Goodwin Powell and Anna Strachan Powell, husband and wife, Appellants vs. Peter J. Wumkes, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Southern District of California Central Division.

Filed November 13, 1943.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
For the Ninth Circuit.

No. 10610

In the Matter of

JAMES GOODWIN POWELL and
ANNA STRACHAN POWELL,
Husband and wife,

Debtors.

STATEMENT OF POINTS ON APPEAL

To The Above Honorable Court,

Appellants hereby designate the following points upon which they intend to rely upon said appeal, as follows:

I.

That the Honorable District Court of the United States erred in reversing the Order of the Concili-

ation Commissioner made and dated April 9, 1943, wherein said Conciliation Commissioner made and entered his Order determining the value of certain property which secured the claim of Peter J. Wumkes.

II.

That the Honorable District Court of the United States erred in reversing the Order of the Conciliation Commissioner made and dated May 18, 1943, wherein said Conciliation Commissioner made and entered his Order denying the Petition of said Peter J. Wumkes for a rehearing of the bankrupts' Petition to Determine Value of Real Property concerned in said proceedings.

III.

That there was insufficient evidence to justify the foregoing decisions of the District Court of the United States, or either of them.

IV.

That the decisions of the District Court of the United States were contrary to the law made and propounded for such matters.

V.

That said District Court admitted and considered improper and illegal evidence in the making of said decisions, and each of them, to-wit, the admission of offer to purchase made by one Louis A. Turner, and offers by John Curci, K. C. O'Bryan, and others.

VI.

That said Honorable District Court erred in reversing the Conciliation Commissioner's Order of May 18, 1943, in that said Petition for a Rehearing of the bankrupts' Petition to Determine Value of Real Property did not state sufficient facts to warrant the granting of a rehearing of said bankrupts' Petition.

VII.

That the above said Orders of the Conciliation Commissioner were made within the discretion of said Commissioner and that said Honorable District Court erred in reversing said Orders.

Dated this 24 day of November, 1943.

H. R. GRIFFIN
Attorney for Debtors and
Appellants.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed Nov. 26, 1943. Paul P. O'Brien, Clerk.

No. 10610

In the United States
Circuit Court of Appeals
For the Ninth Circuit

JAMES GOODWIN POWELL, and ANNA STRACHAN POWELL, husband and wife,
Appellants,

vs.

PETER J. WUMKES,
Appellee.

Appellants' Opening Brief

H. R. GRIFFIN,
Katz Building,
San Bernardino, California
Attorney for Appellants.

Barnum & Flagg Company, San Bernardino, California

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No. 10610

In the United States
Circuit Court of Appeals
For the Ninth Circuit

JAMES GOODWIN POWELL and ANNA STRACHAN POWELL, husband and wife,
Appellants,

vs.

PETER J. WUMKES,
Appellee.

Appellants' Opening Brief

RECORD ON APPEAL

This proceeding is to review the decisions of the Honorable Yankwich, Judge of the United States District Court, reversing the order of the Conciliation Commissioner of San Bernardino County, dated April 9, 1943, wherein said Conciliation Commissioner made and entered his order determining the value of certain property which secured the claim of Peter J. Wumkes, and also reversing the Order of the Conciliation Commissioner made and dated May 18, 1943, wherein said Commissioner denied the Petition of Peter J. Wumkes for a rehearing of the bankrupts' Petition to determine value of real property.

The Record on Appeal contains the complete record and all of the proceedings and evidence in the above-entitled matter. (T-127). Said transcript of record is herein referred to by the letter "T" and its pages by their numbers.

JURISDICTION

The right of the Court to review the Orders of the Conciliation Commissioner has been repeatedly recognized. Perhaps one of the more recent cases on this point is Rait v. Federal Land Bank of St. Paul. (135 Fed. 2d. 447).

STATEMENT OF THE CASE

Appellants, Powell and his wife, were engaged in farming operations, to-wit, growing citrus products. The property consisted of two adjoining parcels of land, one approximately 4.2 acres in size planted to citrus trees, with a house, garage, poultry house thereon, etc., being encumbered with a Trust Deed in favor of Frank Clark, and the second parcel adjoining the Clark property consisting of approximately 5-7/8ths acres planted to citrus and encumbered by a Trust Deed in favor of Peter J. Wumkes. (T-70). (For purposes of clarity, reference to each grove hereafter will be by the use of descriptive words such as "Clark Grove or Wumkes Grove." For purposes of brevity, parties may be referred to hereafter by the use of last name, such as, "Powell, Clark or Wumkes.")

On the 25th day of July, 1940, Powells filed their Petition and schedules. (T-2-17), the debts consisting of the taxes, trust deeds on the property, a small balance on a car, but no other debts. (T-5-8). Thereafter the proceedings were referred to Hon. Fred Duffy, United States

Conciliation Commissioner for the County of San Bernardino. (T-17). Having been unable to secure acceptance or confirmation of an extension proposal, Powells then filed their amended Petition and on October 24, 1940, were adjudicated bankrupts under Section 75(s) of the Bankrupt Act. (T-18). Thereafter and on June 16, 1941, the Commissioner made his order staying proceedings for three years and fixing the rental for said property.

On December 23, 1942, Powells filed a Petition requesting reappraisal or hearing to determine value of the real property. (T-107), and on January 20, 1943, notices were mailed, to each creditor shown by the schedules, of Hearing on Petition to Determine Value of Debtors Real Property, to be heard on February 2, 1943, at ten o'clock A. M., at the Commissioner's office. (That notice of said hearing to said Peter J. Wumkes was returned with the notation "Moved, left no address"). That, however, a few days prior to the second of February, 1943, on request of attorneys for Peter J. Wumkes, said hearing was continued by the Commissioner to the 16th of February, 1943. And then another continuance was asked by Peter J. Wumkes' attorneys and on February 16th, the Commissioner took the matter off the calendar and re-set it for Wednesday, March 3, 1943, mailing new notices of hearing. (T-105). (By way of explanation, the Commissioner had received a communication from Hon. Garfield R. Jones, Supervising Conciliation Commissioner, that Peter J. Wumkes had contacted a Deputy United States Marshall who contacted Mr. Jones who then contacted Mr. Wumkes and then Mr. Jones had in writing to this Commissioner furnished the Commissioner with the then address of said Peter J. Wumkes.) (T-42).

That on the 3rd day of March, 1943, at the time and place set, appeared the debtors and their attorney, H. R. Griffin, Clark and his attorney, Henton S. Brennan, and Dr. Peter J. Wumkes and his attorney, Russell Goodwin. Prior to the hearing and before the appearance in Court of said Peter J. Wumkes, said attorney Russell Goodwin requested the Commissioner to allow him to withdraw as attorney for Peter J. Wumkes but the request was denied. Again, at the beginning of the hearing and before testimony had been offered, said Goodwin requested the Commissioner to be allowed to withdraw as attorney for Dr. Wumkes and with the consent of Dr. Peter J. Wumkes the request was granted. (T-43).

The matter then proceeded to hearing and evidence both documentary and oral were received. Dr. Wumkes was present during the taking of all testimony, and was by the Commissioner asked if he cared to examine each witness produced, was asked if he had any evidence to introduce and in each case replied in the negative and refused to ask any witness any questions or to testify himself or produce any evidence. At the close, the matter was submitted and on the 25th of March, 1943, the Commissioner rendered his decision (T-79), and mailed notice thereof (T-43-44). On April 2nd the Commissioner made his Findings of Fact and Conclusions of Law and served notice thereof, and on April 9, 1943, signed said Findings and Conclusions. (T-44).

On April 15th Clark filed a Petition for review but on May 11th withdrew such Petition. (T-57).

On April 20th, Wumkes filed a Petition for rehearing to determine value of real property. (T-36), and after notice thereof, said Petition was heard on May 18, 1943, with

Powell and his attorney, H. R. Griffin, and Petitioning Creditor Wumkes not being personally present but represented by his attorneys, Nichols, Cooper and Hickson, by Donald P. Nichols, no evidence was produced by the Petitioner. (T-24). Russell Goodwin, former attorney for Wumkes, was present and testified that the last address and only address of Wumkes that he knew was 922 E. Lugonia Avenue, Redlands, California. That Wumkes had at one time furnished him, the said Goodwin, a telephone number, Arizona 9-3551, Los Angeles, to call him at, that he, the said Goodwin, called said number on February 13, 1943, and was informed by telephone operator that no such number existed and no name listed thereunder. That said Goodwin exhibited and left with the Commission two envelopes, one bearing postmark dated February 12, 1943, and another being postmarked February 13, 1943, which said envelopes were addressed to Dr. Peter J. Wumkes, 922 E. Lugonia Avenue, Redlands, and had been returned marked "Gone, moved, left no address." (T-25. 31). On the 18th day of May, 1943, said Petition was denied. (T-34).

That various extension orders were granted and on June 11, 1943, Wumkes filed a Petition to review the Order of the Commissioner made on May 18, 1943 (T-26), and on June 11, 1943, said Wumkes also filed a Petition to review the Commissioner's Order of April 9, 1943.

Upon the hearing before the Hon. Leon R. Yankwich, the Order of the Commissioner made April 9, 1943, determining the value of the real property was reversed and the Order of the Commissioner made May 18, 1943, wherein the Commissioner denied the Petition of Wumkes for a rehearing to determine value was reversed and the matter

referred back to the Conciliation Commissioner for a further hearing, and that said Wumkes should pay as a condition precedent the sum of $50.00 to the attorney for the Powells. (T-121-122), and from this Order and judgment of the Hon. Leon R. Yankwich, this appeal was taken.

STATEMENT OF POINTS ON APPEAL

To the Above Honorable Court.

Appellants hereby designate the following points upon which they intend to rely upon said appeal, as follows:

I.

That the Honorable District Court of the United States erred in reversing the Order of the Conciliation Commissioner made and dated April 9, 1943, wherein said Concliation Commissioner made and entered his Order determining the value of certain property which secured the claim of Peter J. Wumkes.

II.

That the Honorable District Court of the United States erred in reversing the Order of the Conciliation Commissioner made and dated May 18, 1943, wherein said Conciliation Commissioner made and entered his Order denying the Petition of said Peter J. Wumkes for a rehearing of the bankrupts' Petition to Determine Value of Real Property concerned in said proceedings.

III.

That there was insufficient evidence to justify the foregoing decisions of the District Court of the United States, or either of them.

IV.

That the decisions of the District Court of the United States were contrary to the law made and propounded for such matters.

V.

That said District Court admitted and considered improper and illegal evidence in the making of said decisions, and each of them, to-wit, the admission of offer to purchase made by one Louis A. Turner, and offers by John Curci, K. C. O'Bryan, and others.

VI.

That said Honorable District Court erred in reversing the Conciliation Commissioner's Order of May 18, 1943, in that said Petition for a Rehearing of the bankrupts' Petition to Determine Value of Real Property did not state sufficient facts to warrant the granting of a rehearing of said bankrupts' Petition.

VII.

That the above said Orders of the Conciliation Commissioner were made within the discretion of said Commissioner and that said Honorable District Court erred in reversing said Orders.

ARGUMENT

Perhaps to approach this matter from a more logical basis and one from point of time, let us first discuss the Order of the District Court reversing the Order of the Conciliation Commissioner of May 18, 1943, denying the Petition of Wumkes for a rehearing of the bankrupts' Pe-

tition to determine value. So far we have not been able to find authorities bearing directly on this question but it would appear to us that the situation is very similar to a motion for a new trial. Perhaps not entirely so, for in bankruptcy matters it is not unusual and perhaps the common thing for creditors either not to appear or to appear without counsel and yet commissioners still ascertain and determine the facts as presented and render their decision.

In this case it is clearly shown that the hearing was set for February 2nd, notices mailed and at the request of the attorneys for Wumkes was continued, to February 16th, and again at Wumkes' attorneys' request continued and re-set for March 3rd, and new notices sent, then on March 3rd Wumkes and his attorney appeared and Wumkes consents to the withdrawal of his attorney. No request for a continuance is asked, no statement is made regarding notices or otherwise, the Commissioner asked if they were ready to proceed (T-46), and no negative answer was given, thereupon four appraisers of experience and standing told of their examination of the two properties both adjoining each other, presented photographs, told of water, soil, condition of the trees, houses and buildings, and gave their opinion of the value of the property. Two of the appraisers set the value of the Wumkes property at $3,900.00 and $3,600.00; the adjoining Clark property which included a house, poultry house, buildings, garage, etc., at $4,150.00 and $3,525.00; the other two appraisers set the value of the Clark property at $6,050.00 and $5,500.00. (T-74-77).

While Dr. Wumkes sat throughout the hearing without objection or request for continuance and then waiting until after the court entered its Findings and Conclusions and

Order, thus gambling on what might happen, then on the 20th day of April, nearly seven weeks after the hearing, Wumkes filed his Petition for a rehearing, not denying that he had received notice but merely alleging he had attempted to contact his attorney, Russell Goodwin, had left his phone number and had not heard from him, the said attorney Goodwin. Stated further, he believed his attorney had obtained witnesses to assist the court in determining value and the attorney had not, that he consented to his attorney's withdrawal but although afforded the opportunity he was without legal experience and did not know what questions to ask. That by mistake and excusable neglect, he was not afforded the opportunity of subpœning witnesses. (T-38).

In other words, and in brief, a motion for a rehearing on the sole ground of mistake and excusable neglect, as the affidavit itself terms it. (T-38).

"There is no such ground for granting a new trial as mistake or inadvertence, as distinguished from accident or surprise." Fincher v. Malcolmson, 96 Cal. 38, at pg. 41.

Fed. Rule of Civil Procedure, Rule 59 (a-2), 28 U. S. C. A. 723C at pg. 723: "A new trial may be granted to all or any of the parties and on all or any of the issues: (1) In jury cases . . .; (2) In actions without jury, for any of the reasons for which rehearings have heretofore been granted in suits in equity in the courts of the United States.

The common grounds being (1) Error of law, or fact on face of record; (2) Newly discovered evidence. 3. Moore Federal Practice, pg. 3247.

Generally, to authorize the granting of a motion, the accident or surprise claimed must be such that ordinary

prudence could not have guarded against it." 20 Cal. Jur. 26.

Surprise has been defined as "Some condition or situation in which a party to a cause is unexpectedly placed, to his injury, without any default or negligence of his own, which ordinary prudence could not have guarded against." 20 Cal. Jur. 67. These principles are so generally accepted that we are not citing more specific authorities. As a general rule where surprising conditions arise upon a trial, the party whose rights are materially affected thereby should, at the earliest practicable moment, apply for such relief as will produce the least vexation, expense or delay, either by non-suit, a continuance, the introduction of other evidence or some other available mode. Such a party may not remain silent, taking his chances upon a favorable verdict, and thereafter move for a new trial. 20 Cal. Jur. 74, Schellhous v. Ball, 29 Cal. 605.

In the recent case of Barlow v. Federal Land Bank of Berkeley C. C. H. Bankruptcy Law Service, 1943 No. 54, 636 at pg. 55,739; 139 Fed. (2d) 96, the property had been appraised, the debtor given forty days to redeem after the time to redeem, the debtor filed a Petition asking that the appraisal be reviewed and the court find the true value of the property. The court denied the Petition and ordered the abandonment of the property. In that case the court said:

> "Appellant had forty days to redeem at the appraised value, but he did nothing. He sat for ninety days and did nothing. Then he came into court and asked the court to review the appraisal and if found incorrect that the court fix the true value of the property. There is even no charge that the appraisal was

> fundamentally erroneous. The most serious charge was that no hearing was had on the appraiser's report and that he had no opportunity to object to it. He had an opportunity to object when the report was lodged in court. He failed to make any objection during the forty day period fixed for redemption and for fifty days thereafter. Such dilatory tactics and delay may not be condoned."

Again in the case of in RE ADVOCATE C. C. H. Bankruptcy Law Service, No. 54, 519, August, 1943, D. C., N. Y., at pg. 55, 596, a motion by a bankrupt to be allowed to review a turnover order was denied because the court said the affidavit showed a plain and inexcusable delay in seeking a review without the presentation of any sound reason for the granting of the motion, and the court further said:

> "This is a motion where the delay of the bankrupt . . . is not only inexcusable but is one where the discretion of the court would be abused in granting it."

Examine the Petition of Peter J. Wumkes, has he excused his failure to see his attorney, note that he had moved to West Wood Village (T-105) which is West of Los Angeles, did he come to Redlands to consult with his attorney, had he given his attorney a correct address to write to? Apparently from the record the order staying proceedings and fixing rental was made in June, 1941 (T-68) and the matter was dormant thereafter. Is it not the duty of a client to keep his attorney and the court advised if he moves out of the city and the county? Can a party after receiving notice of a Federal hearing ignore the matter, negligently fail to seriously attempt to contact his attorney, have two continuances granted his attorney, and yet be said to

have exercised ordinary prudence or diligence and be innocent of negligence? Can he expect his attorney to obtain expert witnesses not knowing where his client was or his wishes and without any allegation or proof of the payment of cost to permit the attorney so to do?

We submit that such a Petition does not show accident or surprise, that the exercise of ordinary prudence could not have guarded against. Nor was he placed in such a position without negligence of his own. We, therefore, respectfully contend that the Honorable District Court erred in reversing the Commissioner's Order of May 18th, in that said Petition for said rehearing did not state sufficient facts to warrant the granting of a rehearing of said bankrupts' Petition, that there was insufficient evidence to justify his decision and that said decision was contrary to the law made and propounded for such matters.

THAT THE HONORABLE DISTRICT COURT ERRED IN REVERSING THE ORDER OF THE CONCILIATION COMMISSIONER MADE APRIL 9, 1943, DETERMINING THE VALUE OF CERTAIN PROPERTY.

Now considering the reversal of the Commissioner's Order of April 9th, determining the value of the property. An examination of the record clearly shows that four appraisers testified before the Debtor Powell as to the value of the property. Mr. Aubry, a licensed Real Estate Broker, Appraiser, and former District Manager of Farm Security Administration for Riverside and San Bernardino Counties, former land bank appraiser for Southern California, real estate broker appraising Citrus properties in San Bernardino, Riverside, Ventura, Orange and Los Angeles and other counties, having formerly appeared

before the Federal Court; Mr. W. H. Johnson, connected with Redlands Yucaipa Land Company for ten years, living in Redlands thirty-two years, with years of experience as an appraiser; G. D. Inman, Real Estate Broker since 1929 in Redlands; James Wheat, a former Postmaster of Redlands and engaged in the Real Estate business, all outstanding men, and the record shows that they took into account and described on the witness stand such various elements entering into the value of the property involved as its location, topography, soil formation and quality, existence of depreciating defects and blemishes, nature and condition of the improvements, etc., these being the factors particularly spoken of in the case of Equitable Life Assurance Society of the United States v. Carmody 131 Fed (2d) 318, that evidence of production was also introduced as in the case of in Re Alberti 41 Fed. Supp. 380, C. C. H. Bankruptcy Law Service No. 53, 429, at pg. 53, 677, decided by Judge Yankwich, but as in the Carmody case where the court said:

> "The situation here is hardly identical with that presented in Re Alberti where the court said 'This review presents the very simple question whether agricultural property can be appraised legally by taking into consideration one factor only, namely, productivity, under the use to which it is being put.' In the present case the witnesses for Appellant and those for the Debtor clashed sharply in their description and judgment of many of the value factors, such as the condition of the soil and the improvements, and the Conciliation Commissioner was, of course, required to resolve the question of credibility under the various elements detailed. He was entitled, however, to determine the fact as to each specific element, as he believed it to exist from

the testimony, and to use all of such facts, together with such light as he felt was soundly contributed by the varying arithmetical estimates of the witnesses in formulating his own judgment as to the actual market value of the property, and on the record before us, we cannot say, nor do we have any reason to believe that he was applying a false standard or criterion of market value, such as the court held had been done in the Alberti case."

THAT THE ORDERS OF THE CONCILIATION COMMISSIONER WERE MADE WITHIN HIS DISCRETION AND THAT THE HONORABLE DISTRICT COURT ERRED IN REVERSING SAID ORDERS.

Both of the Orders made by the Commissioner came within his discretion and the cases clearly point out that the court should not interfere with the trial court's discretion unless there is a gross abuse thereof. In the case of Dunsdon v. Federal Land Bank of St. Paul, C. C. H. Bankruptcy Law Service, 54, 445 at pg. 55, 531; 137 Fed (2d) 84, the court said:

> "It is the duty of the District Court to accept the Conciliation Commissioner's findings as to value, based upon a hearing, unless he is soundly convinced from the proceedings before him that it is clearly erroneous. Equitable Life Assurance Society of United States v. Carmody, 131 Fed. (2d) 318, 323. Again, in RAIT—Federal Land Bank of St. Paul, 135 Fed. (2d) 447, we emphasized that the value duly fixed upon a farmer's debtor's property, after a hearing of the Conciliation Commissioner, should not lightly be disturbed, and that the District Judge ought to proceed with a sound and conscientious restraint, before overturning it on review."

Again, in the Carmody case the court said:

> "In a proceeding of the character here involved, where there has been only a review of the previous record and no additional evidence has been received, the law clearly does not contemplate that a finding of the Conciliation Commissioner shall be set aside by a District Judge on a mere difference in personal judgment as to the crediting of the record evidence."

Certainly the Commissioner who heard the motion for a rehearing and also the testimony at the hearing determining value had a greater opportunity to judge the credibility of the witnesses and to determine not only value in the one instance but in the other instance, if a rehearing should have been granted because of surprise or accident, that the exercise of ordinary prudence and diligence could not have guarded against.

THE DISTRICT COURT ADMITTED AND CONSIDERED IMPROPER AND ILLEGAL EVIDENCE IN THE MAKING OF SAID DECISIONS, AND EACH OF THEM, TOWIT, THE ADMISSION OF OFFERS TO PURCHASE MADE BY ONE LOUIS A. TURNER, AND OFFERS OF JOHN CORCI, K. C. O'BRYAN, AND OTHERS. (T-113, 114, 115, 120).

The admissibility of offers of purchase has been considered by the court. Perhaps one of the leading cases is the case of Sharp v. United States, 191 U. S. 341; 48 Law. Ed. 211. There that court said:

> "Upon principle, we think the trial court was right in rejecting the evidence. It is, at most, a species of indirect evidence of the opinion of the person making such offer as to the value of the land. He may have so slight a knowledge on the subject as to render his

opinion of no value, and inadmissible for that reason. He may have wanted the land for some particular purpose disconnected from its value. Pure speculation may have induced it, a willingness to take chances that some new use of the land might, in the end prove profitable. There is no opportunity to cross-examine the person making the offer, to show these various facts. Again, it is of a nature entirely too uncertain, shadowy, and speculative to form any solid foundation for determining the value of the land which is sought to be taken in condemnation proceedings. If the offer were admissible, not only is it almost impossible to prove (if it exists) the lack of good faith in the person making the offer, but the circumstances of the parties at the time the offer was made as bearing upon the value of such offer may be very difficult, if not almost impossible to show. To be of the slightest value as evidence in any court, an offer must, of course, be an honest offer, made by an individual capable of forming a fair and intelligent judgment, really desirous of purchasing, entirely able to do so, and to give the amount of money mentioned in the offer, for otherwise the offer would be but a vain thing. Whether the owner himself, while declining the offer, really believed in the good faith of the party making it, and in his ability and desire to pay the amount offered, if such offer should be accepted, or whether the offer was regarded as a mere idle remark, not intended for acceptance, would also be material upon the question of the bona fides of the refusal . . . In our judgment they do not tend to show value, and they are unsatisfactory, easy of fabrication, and even dangerous in their character as evidence upon this subject . . . There is no chance to cross-examine as to the circumstances of the party making the offer in regard to good faith, etc."

In the case at bar, counsel not only criticized the Commissioner because he did not receive such an offer of purchase but the District Court likewise indicated that he felt that such testimony should have been admitted by the Commissioner at the time of the motion for rehearing and considered affidavits of offers of purchase at the time of the hearing in the District Court. This, we contend, was error for such evidence is inadmissible.

The Superior Court of California likewise determined this point, for in the case of the Central Pacific Railway Company of California v. Pearson, 35 Cal. 247 at pg. 262, the court said:

> "But, while the opinions of witnesses thus qualified by their knowledge of the subject are competent testimony, they cannot, upon the direct examination, be allowed to testify as to particular transactions, such as sales of adjoining lands, how much has been offered and refused for adjoining lands of like quality and location, or for the land in question, or any part thereof, or how much the company has been compelled to pay in other like cases—notwithstanding, those transactions may constitute the source of their knowledge. If this were allowed, the other side would have a right to controvert each transaction instanced by the witnesses, and investigate its merits, which would lead to as many side issues as transactions, and render the investigation interminable . . . Greenl. on Ev. Sect. 448"

CONCLUSION

May we, therefore, in closing, submit that this case while arising from the same Conciliation Commissioner is not similar in fact or in law to the case in RE ALBERTI Supra, which was decided by the Hon. Judge Yankwich and which he emphasized and referred to repeatedly in this case, that as in the Carmody case the evidence covered many elements other than productivity and the finding of the Commissioner was proper. That in addition, that certainly some duty and some responsibility is placed upon a party who receives a notice of the setting of a matter before a Federal Conciliation Commissioner, that party cannot be lax and dilatory and then expect the court to aid him and grant a rehearing of the case. We, therefore, respectfully urge that the Orders made by the Conciliation Commissioner were proper and should have been upheld by the District Court.

Respectfully submitted,

H. R. GRIFFIN,
Attorney for Appellants.

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No. 10610.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

JAMES GOODWIN POWELL and ANNA STRACHAN POWELL, husband and wife,

Appellants,

vs.

PETER J. WUMKES,

Appellee.

APPELLEE'S BRIEF.

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FOR THE NINTH CIRCUIT

JAMES GOODWIN POWELL and ANNA STRACHAN POWELL, husband and wife,

Appellants,

vs.

PETER J. WUMKES,

Appellee.

APPELLEE'S BRIEF.

Preliminary Statement.

The "Statement of the Case" contained in Appellants' Opening Brief (pp. 2 to 6) is substantially a correct statement of the factual background upon which Appellants seek to reverse the judgment of the District Court with the following exceptions consisting of certain corrections and additions. The first correction is the manner in which the so-called "opportunity" of examining witnesses and presenting evidence is presented by the Appellants in the "Statement of the Case": the next correction is the assertion by the Appellants that at the hearing of May 18, 1943, the Appellee produced no evidence.

With respect to the said "opportunity" to examine witnesses and produce evidence, the "Statement of the Case" is more eloquent in what it leaves unsaid than in those matters which the Appellants present as conclusions from what actually occurred. The transcript of the record shows affirmatively by the Commissioner's Certificate that the Appellee was by the Commissioner "asked if he cared to examine each witness produced; was asked if he had any evidence to introduce. In each case he answered in the negative and refused to ask any witness any questions or to testify himself or produce any evidence" [Tr. p. 44], this apparently being the conclusion of the Commissioner as to what actually occurred, but the Commissioner in his zeal to explain the "fairness" of his hearing, also inserted in the Certificate the evidence from which his said conclusion was drawn. It is shown in the following words of the Commissioner:

> "* * * (After the withdrawal of Russell Goodwin as attorney for Peter J. Wumkes, as hereinbefore shown, this Commissioner said: 'This is the time and place fixed for the hearing of petition to determine value of debtor's real property. Are you ready to proceed?' No negative answer was interposed.)" [Tr. p. 46.]

The Commissioner first correctly recognized the danger of proceeding without Mr. Wumkes being represented [Tr. p. 43], then fell into the error of permitting said counsel to withdraw [Tr. p. 44] without giving the Appellee a chance to obtain other counsel, and proceeding without advising Mr. Wumkes concerning his rights to have coun-

sel, to seek or obtain a continuance for the purpose of obtaining counsel, or himself undertaking to protect the said creditor's rights, as, under such circumstances, he may well be duty bound to do, and without any substitution of the Appellee *in propria persona* for Russell Goodwin, Esq.

Parenthetically, we challenge the Commissioner's recital contained in his Findings of Fact, Conclusions of Law [Tr. p. 65] and Decision [Tr. p. 75], stating that the Appellee Peter J. Wumkes appeared "personally and through his attorney, Russell Goodwin, Esq.," as a litigant either appears personally, that is to say: *in propria persona* or by counsel, and never in both capacities. (Rules of U. S. District Court, Rule 1 (d), (e), (2), (3).)

It appears that at the hearing of May 18, 1943, had before the Commissioner, although the Commissioner's Certificate states that "no evidence to sustain allegations of petition for rehearing" was introduced, nevertheless, the Commissioner took some wholly irrelevant testimony from Russell Goodwin, Esq., the attorney whom he permitted to withdraw from the proceeding during the previous hearing, and it appears further by the Transcript that although the Appellee was ready with testimony bearing upon the matters in issue, the Commissioner refused to hear the parties other than the attorney who had previously withdrawn. [Affidavit of Donald P. Nichols, Tr. p. 119.]

Three additional facts which are excluded from the "Statement of the Case" contained in Appellants' Opening Brief, require attention:

First: It appears that the Commissioner made a rent order under Subsection (s) of Section 75 of the Bankruptcy Act on June 16, 1941 (App. Op. Br. p. 3), consisting of one-fourth of the gross proceeds of the income produced on the agricultural real property of said Appellants [Tr. p. 28], and that none of said rent was paid [Tr. p. 28], and that the Commissioner refused to give Appellee any accounting or any statement concerning any of said monies [Tr. p. 119] and his order granting the Appellants the right to obtain the property free and clear of the $12,000.00 existing encumbrance for the sum of $3,900.00, failed to take into account any portion of said rent. [Tr. pp. 75 and 76.]

Second: Both of the Appellants themselves considered the value of the farm upon which the Appellee, Peter J. Wumkes, held his deed of trust, to be the sum of $8,000.00 [Tr. p. 8], and such value was placed upon said property under oath by each of said Appellants with H. R. Griffin, counsel for the Appellants taking the oath of said Appellants to the accuracy and correctness of such value. [Tr. p. 15.]

Third: Either by reason of the general change in economic conditions with a substantial increase in prevailing prices for farm products, or the sudden and unexpected improvement in the condition of this "marginal" grove, resulted in a net packinghouse return to the Appellants on the Wumkes' grove for the season 1941-42 in the sum of $3,287.06. [Tr. pp. 70-100.]

ARGUMENT.

The District Court Did Not Err in Reversing the Commissioner's Order of April 9, 1943.

(A)

The District Court, in Determining the Correctness and Fairness of the Commissioner's Order of April 9, 1943, Had Before It Facts Which the Commissioner Also Had Before Him, but Which He Ignored and Failed to Consider.

First: The value as placed upon the real property in question by both of the Appellants as late as July 20, 1940, which appeared to have been the sum of $8,000.00.

Second: The fact that the ranch for a period of four years continually improved in the yield until in the season of 1941-42, it produced oranges, giving to the Appellants a net packinghouse return of $3,287.06.

Third: The general improved economic conditions affecting the orange industry generally, of which the Commissioner must have known, and which constituted a portion of the facts of such general notoriety, as not to require proof, but which the Commissioner ignored and failed to consider.

Olson v. United States, 292 U. S. 246, 257, 78 L. Ed. 1236, 1245.

(B)

The District Court Had Before It on Such Review Additional Facts Which Supported Its Action in Reversing the Judgment of the Commissioner and Justified the District Court in Exercising Its Discretion in Remanding the Case to the Commissioner for Further Proceedings.

First: The Appellee introduced the sworn testimony of Mr. L. A. Turner, engaged in the orange business since 1925, showing the value on March 1, 1943, to have been $8,500.00. [Affidavit of L. A. Turner, Tr. p. 109.]

Second: The Appellee introduced the sworn testimony of Peter J. Wumkes showing, among other things, that the Appellants, James Goodwin Powell and Anna Strachan Powell, considered the property to have a value of $13,-500.00, in the year 1938, on which date he sold to said Appellants the said parcel of property for $13,500.00; $2,500.00 cash, down payment, and the balance secured by trust deeds against the property, and that said creditor has received no payments of any kind on account of the rental order made by the Commissioner on the 16th day of June, 1941, and that he considered the value of the property in 1943 to be the sum of $10,000.00. [Affidavit of Peter J. Wumkes, Tr. pp. 116-117.]

Third: The Appellee introduced the sworn testimony of Donald P. Nichols that the Commissioner refused to take any testimony on the Appellee's petition for reappraisal of the property, and that the Commissioner refused to give any statement or accounting whatsoever, and further refused to make any statement that he had as a matter of fact paid nothing on account of the rental monies received, or ordered paid, by him. [Affidavit of Donald P. Nichols, Tr. p. 119.]

Fourth: The Appellee also introduced the sworn testimony of K. C. O'Bryan, President of Southern Citrus Association, owner of numerous citrus properties in the vicinity, who placed the value of the grove at $8,000.00, and was incidentally willing to pick up a bargain by offering $6,500.00 cash therefor. [Affidavit of K. C. O'Bryan, Tr. p. 113.]

(C)

The Applicable Law.

General Order No. 47, established by the Supreme Court pertaining to hearings by referees, as amended February 13, 1939, provides:

> "Unless otherwise directed in the order of reference the report of a referee or of a special master shall set forth his findings of fact and conclusions of law, and the judge shall accept his findings of fact unless clearly erroneous. The judge after hearing may adopt the report or may modify it or may reject it in whole or in part or may receive further evidence or may re-commit it with instructions."

Apart from the propriety of the Commissioner granting to the debtors the right to obtain title to the real property upon which the Appellee held an encumbrance in excess of $12,820.15 [Tr. p. 4], for the sum of $3,900.00 [Tr. p. 76], at a time when no rental payments had been made (*In re Ryder,* 40 Fed. Supp. 882), the Courts have in numerous decisions affirmed and reaffirmed the power of the District Court in adopting or refusing to adopt the findings of a referee on the question of value.

In re Byrd Coal Co., 83 Fed. (2d) 190;

In re West Produce Corp., 118 Fed. (2d) 274;

In re Duvall, 103 Fed. (2d) 653.

While there can be no question that the District Court may act improperly in substituting its judgment for that of the referee where he does not receive any further evidence (*Dunsdon v. Federal Land Bank of St. Paul,* 137 F. (2d) 84), and wherein he is not convinced that the Commissioner's finding as to value is clearly erroneous (*Equitable Life Assur. Soc. etc. v. Carmody,* 131 F. (2d) 318), nevertheless, it appears that the District Court is not "utterly helpless in any case to deal with a specific situation, simply because the record submitted to him on review meets the mechanical tests and standards" provided in the statute and expounded in the decisions. *(Dunsdon v. Federal Land Bank etc., supra.)* The Circuit Court correctly recognizes the pernicious results that may follow the adoption of the rule urged by the Appellants herein by stating:

> "Situations may exist where, in the interest of justice, he may soundly exercise a discretion to receive or require additional evidence in connection with a review of a conciliation commissioner's order, and determine from the entire record thus before him whether a correct result has been reached."
>
> *Dunsdon v. Federal Land Bank, supra.*

There can be no comfort to the Appellants in either of the cases that they so heavily rely upon to reverse the order of the District Court. *(Dunsdon v. Federal Land Bank* and *Equitable Life Assur. Soc. etc. v. Carmody, supra.)* Indeed, it may not be amiss to recognize the distinction that exists between the powers and duties of the District Court in acting upon a review of the Referee's findings and the Circuit Court, in passing upon the correctness of a District Court's determination.

The Circuit Court of the Eighth Circuit, in the case of *Rait v. Federal Land Bank of St. Paul,* 135 F. (2d) 447, states the distinction as follows at page 540:

> "* * * But where, from a review of the record and from such other proceedings as may be had before him, the district judge, on the basis of the principles referred to, is clearly convinced that the conciliation commissioner in such a situation has acted arbitrarily and without proper regard for the evidence, or that he has otherwise plainly and prejudicially erred, there can be no question as to his right to modify the conciliation commissioner's report or order, or to set it aside and receive further evidence, or to recommit the matter to the conciliation commissioner with instructions."

And at page 541:

> "* * * Our only power and duty in the situation presented here are to test whether the result which now has been reached by the district judge's exercise of his authorized functions is itself clearly erroneous. Rule 52(a), Federal Rules of Civil Procedure, 28 U. S. C. A., following section 723c. On the record before us, we cannot declare the value fixed by the district judge to be clearly erroneous. The fact that some other equally sustainable result might have been reached on the evidence is beside the point."

The rule applicable following the reversal of a referee's decision by the District Court is that the decision of the District Judge is presumptively correct.

Wilson v. Hall, 81 Fed. (2d) 918.

The "substantial evidence" rule used in determining an appeal from the District Court has no application in the

exercise of the discretion vested in the District Judge on review of a referee's determination.

In re Duvall, 103 Fed. (2d) 653.

Appellee respectfully submits that in the state of the record herein shown, the District Court correctly exercised a sound discretion in reversing the decision of the Commissioner in this respect, and remanding the matter for further consideration.

Appellee could not present any better argument than the words of the Circuit Court in the case of *Kauk v. Anderson,* 137 Fed. (2d) 331, at pages 333 and 334, wherein it states:

> "The district judge in a case such as this must first decide whether the conciliation commissioner has competently tried and competently determined the issue of value. If he has, his determination should stand. If he has not, then the district judge must decide whether to modify the commissioner's valuation upon the evidence in the record, whether to set the order aside and receive further evidence, or whether to recommit the matter to the conciliation commissioner with instructions. * * * The record on review may afford a sound and sufficient basis for a determination of value by the district judge and therefore justify a modification of the commissioner's valuation. Unless the record does furnish such a basis, we think that the proper course for the district judge to pursue is either to take additional evidence and then determine the issue from the evidence as supplemented or to remand the case to the commissioner with directions to retry the issue of value, pointing out to him the errors which invalidated his previous determination."

The District Court Did Not Err in Reversing the Commissioner's Order of May 18, 1943.

If the District Court, in the exercise of sound discretion, correctly reversed the order of April 9, 1943, it likewise correctly used its discretion in reversing the order of May 18, 1943. It is elementary that the courts will favor the determination of disputed questions of fact on the merits rather than by default.

Underwood v. Underwood, 87 Cal. 525;

Douglas v. Todd, 96 Cal. 655;

O'Brien v. Leach, 139 Cal. 220;

Stone v. Williams, 43 Cal. App. 490;

Bruskey v. Bruskey, 4 Cal. App. (2d) 472;

Kent v. County Fire Ins. Co., 27 Cal. App. (2d) 340;

Re Moreland's Estate, 49 Cal. App. (2d) 484;

Potts v. Whitson, 52 Cal. App. (2d) 199;

Grady v. Donohoo, 108 Cal. 211;

Marshal v. Holmes, 141 U. S. 589, 35 L. Ed. 870.

In fact, under the record submitted in the instant matter, it can reasonably be questioned whether the Commissioner complied with the constitutional mandate of due process.

> "A full hearing is one in which ample opportunity is afforded to all parties to make, by evidence and argument, a showing fairly adequate to establish the propriety or impropriety, from the standpoint of justice and law, of the step asked to be taken."
>
> 12 *Amer. Juris.* 303.

"A person has the right to be present at the hearing in person and represented by counsel. The right to a hearing includes the right to aid of counsel."

12 *Amer. Juris.* 307.

The shocking result should of itself have warned the Commissioner that the "fairness" and "impartiality" which should be the watchword of judicial determination, was probably lacking.

Apart from these considerations, the petition for re-appraisal was addressed to the Commissioner, both as a request for a new trial and as relief from the judgment or order of the Commissioner upon the mistake, inadvertence, surprise and excusable neglect of the Appellee under Rules 59 and 60 of the Rules of Civil Procedure. Under the Rules of the District Court, as they then existed, the general language of Rule 59 was not necessarily limited to the two grounds mentioned by the Appellants (App. Br. p. 9), but also (1) any irregularity in the proceedings * * * or an abuse of discretion by which the losing party was prevented from having a fair trial, (2) newly discovered evidence, material for the party making the application, which he could not with reasonable diligence have discovered and produced at the trial. Either of these grounds should have been accepted by the Commissioner, as obviously the permitted withdrawal of the Appellee's counsel during the hearing, without giving Appellee an opportunity to obtain other counsel, constituted an abuse of discretion by the Commissioner, and the requested additional hearing, showing the secured lien of the Appellee

to be in excess of $14,000.00 [Tr. p. 40], and the original appraisal on the 24th day of November, 1940, to have been $5,200.00 [Tr. p. 38], the suggested "bargain price" purchase offer of $5,500.00 by the Orange Belt Fruit Distributors [Tr. p. 119], indicated to the Commissioner that a mistake had been made, and that the Appellee had newly discovered evidence material to the issue which he could not have produced at the "expedited" proceeding of April 9, 1943.

These grounds have been recognized by the Federal Courts as constituting adequate grounds to grant a new trial.

> "* * * We are not prepared to hold that the trial judge may not, in the exercise of a sound discretion, at the instance of a party or on his own motion, set aside a verdict or grant a new trial, when he is convinced that, because of some accident, mistake, or misfortune in the conduct of the trial, a new trial is necessary to prevent a failure of justice."
>
> *Norton v. City Bank & Trust Co.*, 294 Fed. 839, 843;
>
> *Kithcart v. Met. Life Ins. Co.*, 119 F. (2d) 497.

Rule 60 of the Rules of Civil Procedure is based upon the third and fourth paragraphs of Section 473 of the California Code of Civil Procedure, and the principles governing the exercise of the Court's discretion are correctly stated in 14 *Cal. Jur.* at page 1075 as follows:

> "From the earliest history of the state to the present time it has been held that the power vested in the

trial courts by section 473 of the Code of Civil Procedure should be freely and liberally exercised to the end that they might mold and direct their proceedings so as to dispose of cases on their substantial merits and without unreasonable delay, regarding mere technicalities as obstacles to be avoided rather than as principles to which effect is to be given in derogation of substantial right. The policy of the law is to have every litigated case tried upon its merits; and it looks with disfavor upon a party who, regardless of the merits of his case, attempts to take advantage of the mistake, surprise, inadvertence, or neglect of his adversary. The discretion of the court ought always to be exercised in conformity with the spirit of the law and in such manner as will subserve rather than defeat the ends of justice."

Accident, surprise and mistake are well recognized reasons for the granting of relief from a judgment or decree.

31 *Amer. Juris.*, Secs. 741, 742 and 743.

"The rule that an attorney's negligence may be imputed to his client and prevent the latter from relying on that ground for opening or vacating a judgment, does not necessarily prevail in the event of an attorney's abandonment of or withdrawal from the case. * * * The rule that the granting or refusing of an application to open or set aside a judgment is, in general, within the sound discretion of the trial court has been applied, or at least recognized, in numerous cases in which the withdrawal from or abandonment of the case by an attorney of one of the

parties was the ground interposed for opening or vacating the judgment."

31 *Amer. Juris.,* Sec. 753.

See

Adams v. Rathbun, 14 S. D. 552, 86 N. W. 629;
Simpkins v. Simpkins, 14 Mont. 386, 36 Pac. 759;
People v. Schulman, 299 Ill. 125, 132 N. E. 530.

Conclusion.

In conclusion it is respectfully submitted that the action of the District Court in reversing the Commissioner and remanding the matter to him for further evidence and determination was in the sound discretion of the judge of the District Court, and that the Court's action was, both in the interests of justice and to prevent a miscarriage of justice, supported by the rules governing the proceedings and the law applicable thereto.

Respectfully submitted,

NICHOLS, COOPER AND HICKSON and
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No. 10610

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Appellee.

Appellants' Reply Brief

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Appellee.

Appellants' Reply Brief

STATEMENT OF THE CASE

It is with some pleasure that Appellants find that Appellee admits that the statement of the case as set forth in Appellants' Opening Brief is substantially correct, for he had attempted to set out the facts without argument, coloring or distortion.

In reference to the two suggested corrections of Appellee, may we point out that the first concerns itself merely with an argument attempting to read into the ordinary opening words of any court, to-wit, "This is the time and place fixed for the hearing of Petition to Determine Value

of Debtors' real property. Are you ready to proceed? No negative answer was interposed." Tr. p. 46."
some guilty feeling of the Commissioner. We submit that such an argument is not persuasive and like the following point raised by the Appellee pertaining to the technical recital of the Commissioner that Wumkes appeared "personally and through his attorney, Russell Goodwin, Esq.," is a play upon words and does not have any bearing upon the merits of the case. May we sugest that the Commissioner's certificates and papers very clearly show his desire to recite all of the facts and to attempt to keep the sequence of events clearly before the court.

Now as to the suggested second correction to the effect that the Commissioner's certificate as to the hearing of May 18, 1943, stating that "No evidence to sustain allegations for Petition for Rehearing was introduced." We submit that the statement is correct for the record clearly shows that Wumkes was not personally present, that Russell Goodwin, former attorney for Wumkes, was present and testified. (Tr. 24). And may we point out that the affidavit of counsel for the Appellee on page 119 of the transcript states that he then presented an offer of purchase in the sum of $5,500.00, in writing, and the Commissioner refused to receive said offer. This was correct, and may we point out here that nowhere in Appellees' brief have they cited any authority or argued the admissibility of an offer of purchase and yet Appellants in their opening brief pointed out that numerous authorities clearly hold such offers to be inadmissible and improper. (Appellants' Opening Brief, pages 15, 16 and 17).

Again Appellee attempts to create an impression that is not sustained by the record, that he was ready then with

testimony bearing upon the issues and the Commissioner refused to hear the parties. I suggest we again examine the Affidavit of Mr. Nichols on p. 119 of the transcript. Other than the offer to buy. No statement is made therein that at the time he had offered any other evidence or testimony. Mr. Nichols does state that after the Petition for review was filed that he requested on several occasions of the Commissioner a statement or or accounting of the disbursement of funds received by the Commissioner but he does not state that he did so at the time of this hearing, and even if such a request had been made, it would not have been evidentiary. Thus clearly Appellee's statement is not correct nor is it borne out by the cited Affidavit.

Perhaps at this point it would be well to point out that at the hearing of May 18, 1943, the Commissioner had only the Petition for a Rehearing (Tr. 24); the testimony of Russell Goodwin concerning the mailing of his letters to Wumkes (Tr. 25); the rejected offer of purchase for a sum of $5,500.00 (Tr. 119); as evidence presented, and that the additional affidavits and offers referred to by Appellee in his brief were dated some four months later in September, 1943, and were not presented to the Commissioner but were presented when the matter was before the District Court.

Now as to the remaining facts which Appellee refers to as additional facts; may we suggest that nowhere is there any hint or charge that the Appellants are in contempt or have not lived up to the rent order of the Commissioner. No citation of authority is given that it is incumbent upon a Commissioner to render an accounting or statement; very clearly the Commissioner's books and records are open to the examination of the creditor and he can learn

the disposition of the entire income of the property and what rental, if any, is payable to him after the payment of the proper charges are made by the Commissioner in accordance with the law. Appellants submit that this point is immaterial and has no bearing upon the right of the Appellants to have the property appraised, nor is there anything in the record to show that the Commissioner did not take into consideration such rental, if there was any.

The second point Appellee suggests was overlooked is an argumentive one referring to a statement in the schedule by Petitioners that the property at that time, to-wit, 1940, was valued at $8,000.00. This value is usually and customarily merely an approximate estimate and certainly would have little evidentiary value as it was some three years prior to the date of the reappraisal hearing.

The third point is regarding the good crop year of 1941-1942. Clearly this was an exceptional year for it was three times greater than the preceding year or the second preceding year and the testimony clearly showed that the following year of 1943 instead of running 3,000 boxes that only 263 boxes plus approximately 305 boxes, or a total of 568 boxes were grown which would only be one-sixth of the bumper crop of 1941-1942.

The fourth point is the affidavit of K. C. O'Bryan presented to Judge Yankwich which again contains an offer of purchase which we have heretofore herein and in our opening statement shown to be improper and inadmissible.

ADMISSIONS IN APPELLANTS' BRIEF

First, referring to the hearing of May 18, 1943, we now find Appellee insisting that his Petition was not only

based upon the ground of mistake and excusable neglect but also on (1) irregularity in the proceeding or abuse of discretion; (2) Newly discovered evidence, material for the party making the application, whcih he could not with reasonable diligence have discovered and produced at the trial. However, nowhere does he answer or attempt to answer the law cited by Appellants in their opening brief that it must be a surprise to which a party is unexpectedly placed, to his injury, without any default or negligence of his own which ordinary prudence could not have guarded against (Appellants' Opening Brief, pp. 10, 11 and 12) and further that he must at the earliest practicable moment apply for such relief, as will produce the least vexation, expense, or delay, either by non-suit, a continuance, the introduction of other evidence or some other available mode. Such a party may not remain silent, taking his chances upon a favorable verdict and thereafter move for a new trial. (Appellants' Opening Brief, pp. 10 and 11 and citations therein.)

Secondly, if for purpose of argument we can assume that the Petition raises the point of new evidence, Appellee admits that he must prove that such new evidence could not with reasonable diligence have been discovered and produced at the trial. See Appellee's Brief, p. 12. Along this line may we call to the court's attention the case of Sun Life Ass'n. Company of Canada v. Budzinski 25 Fed. (2d) 77. Where the court said "The application does not show the testimony now recorded as newly discovered was not by proper diligence available at the trial and, therefore, the application fails to show that legal requisite for the allowance for such a motion." Then if Appellee intended to ask for a rehearing upon the existence of

new evidence it certainly was incumbent upon him to show the new evidence and the fact that it could not by reasonable diligence be presented at the trial court, and yet as we have herein before pointed out, the Petition was submitted to the Commissioner upon the Wumkes' Petition, the testimony of Russell Goodwin concerning his letters of notice to Dr. Wumkes and the rejected offer of purchase. This we feel did not constitute new evidence and certainly nothing was proven to show why such evidence could not have been presented at the trial.

We, therefore, respectfully contend that the very facts show that any accident or surprise suffered by the Appellee's counsel withdrawal from the case was the result of the Appellee's own dilatory and negligent actions in which after receiving notice of a Federal hearing Appellee ignored the matter, negligently failed to contact his attorney and then after the court granted two continuances to his attorney and after sitting throughout the case and waiting a month for the decision he then asked the court some seven weeks after the hearing to retry the matter. Certainly this case makes the language of the court in re ADVOCATE C.C.H. Bankruptcy Law Service, 54, 519, p. 5596, Appellee's Opening Brief, p. 11 applicable, to-wit:

"This is a motion where the delay of the..... is not only inexcusable but is one where the discretion of the court would be abused in granting it."

Now, referring to the three cases cited by Appellee pertaining to accident, surprise and neglect, and particularly found on Appellee's p. 15. Let us examine these cases. First, Adams v. Rathbun, 86 N.W. 629, is one where an attorney without knowledge or notice to his client hired another lawyer to take the case and withdrew himself. The

other lawyer at the commencement of the trial asked for a continuance but the court denied it and later the Appellate granted a new trial. There was no negligence or dilatory actions in this case, they asked promptly for the relief and the continuance was denied. In the case at bar, after two continuances granted and other dilatory actions, the Commissioner eventually went ahead and heard the matter.

The second case, Simpkins v. Simpkins, 36 Pac. 759, was a divorce case; the wife living 1200 miles away was served. Her attorney there contacted local counsel who filed a Demurrer, prepared an Answer and suggested a settlement, said local counsel later refused to file the Answer, demanding that his client settle the case, the Demurrer was overruled and twenty-four hours given to answer and default entered. Wires and letters showed the refusal of the attorney to act but there was no negligence on the part of the defendant. Clearly this case is not like the one at bar for here the attorney for Wumkes wrote numerous letters to his client. The letters were returned, telephone calls were of no avail, Wumkes had negligently left the city, left the County, leaving no address for his attorney. His attorney obtained two continuances, however, Wumkes knew of the hearing for he had contacted the Los Angeles Commissioner and notice had been sent to him but he did not contact his counsel at any time but on the day of the hearing he appeared expecting his counsel to be ready, then permitted his counsel to withdraw and permitted the case to proceed without objecting or asking any delay. He then waited a month for the trial court to enter its decision and seven weeks after the hearing asked for relief. Again, we say, that any accident or surprise was caused solely by his own negligence and dilatory action.

Now the third case, People v. Schulman, 132 N.E. 535 is a criminal one where the attorney was not versed in the rights of the defendant and the crime being an indecent liberty case concerning children was not proven to the court's satisfaction. Clearly this case by its very nature being criminal can not be a guide or authority in the case here presented.

Now referring to the District Court's reversal of the Order of April 9th. Appellee suggests that the Commissioner did not look or ignored certain points which points were merely evidentiary and laid within the discretion of the Commissioner to weigh and determine in arriving at his decision.

Secondly, Appellee suggests that the District Court had additional evidence submitted. Clearly the original sale price to the Powells by Wumkes had little evidentiary value and was known by the Commission, the payment of rental was all within the Commissioner's knowledge, so that the only remaining new evidence was merely cumulative, being testimony of estimates of value. If such cumulative evidence will warrant a new trial or a reversal where is there any finality in these matters? Certainly such evidence was clearly available to the Appellee with the exercise of reasonable diligence at the original hearing.

Again, we recall the language of Rait v. Federal Land Bank, 135 Fed. (2d) 447 "That a value duly fixed after a hearing by the Commissioner should not lightly be disturbed, and the District Court ought to proceed with a sound and conscientious restraint, before overturning it on review" and the language of the Carmody case, 131 Fed. (2d) 318," that the law does not contemplate that a finding of the Conciliation Commissioner shall be set aside by a

district judge on a mere difference in personal judgment as to the crediting of the record evidence."

Therefore, in conclusion, may we submit that no party can be so lax and dilatory and yet expect the court to aid him and grant a rehearing in the case. That further, the findings of the Commissioner as to the value of the property were proper and substantiated by the evidence and should be upheld by the Honorable Court.

Respectfully submitted,

H. R. GRIFFIN,
Attorney for Appellants.

No. 10644

United States
Circuit Court of Appeals
For the Ninth Circuit.

LORIN A. CRANSON,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Transcript of Record

Upon Appeal from the District Court of the United States for the Northern District of California, Southern Division

Rotary Colorprint, 590 Folsom St., San Francisco

No. 10644

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San Francisco, California

Attorneys for Defendant and Appellee

In the United States District Court for the Northern District of California, Southern Division

No. 22168-S

LORIN A. CRANSON,

Plaintiff,

vs.

THE UNITED STATES OF AMERICA,

Defendant.

COMPLAINT TO RECOVER TAXES ILLEGALLY COLLECTED

Comes now plaintiff above named, and for cause of action against the defendant herein alleges as follows:

I.

Plaintiff is a citizen of the United States and a [1*] resident of the City and County of San Francisco, State of California.

II.

On or about March 15, 1937, plaintiff filed with John V. Lewis, as Collector of Internal Revenue of the United States for the First District of California, his income tax return for the calendar year 1936, upon Form 1040 furnished by the Commissioner of Internal Revenue of the United States for that purpose. Said return showed an income tax due for said calendar year 1936 from plaintiff in

*Page numbering appearing at foot of page of original certified Transcript of Record.

the amount of One Thousand Seventeen and 38/100 Dollars ($1017.38), which amount plaintiff paid to said John V. Lewis, as Collector of Internal Revenue of the United States for the First District of California, in installments as follows: On or about March 15, 1937, the sum of Two Hundred Fifty-four and 35/100 Dollars ($254.35); on or about June 15, 1937, the sum of Two Hundred Fifty-four and 35/100 Dollars ($254.35); on or about September 15, 1937, the sum of Two Hundred Fifty-four and 34/100 Dollars ($254.34); and on or about December 15, 1937, the sum of Two Hundred Fifty-four and 34/100 Dollars ($254.34).

III.

On or about March 21, 1938, the Commissioner of Internal Revenue of the United States asserted that additional income taxes in the amount of One Hundred Forty-nine and 48/100 Dollars ($149.48) were owing by said plaintiff for said calendar year 1936. Said sum of One Hundred Forty-nine and 48/100 Dollars ($149.48) was paid by plaintiff on or about March 21, 1938, and interest thereon in the amount of Nine and 21/100 Dollars ($9.21) was paid on April 15, 1938. Both of said payments were made to Clifford C. Anglim, as Collector of Internal Revenue of the [2] United States for the First District of California.

IV.

Said John V. Lewis was the duly appointed, qualified and acting Collector of Internal Revenue of the United States for the First District of Cali-

fornia during all the times herein mentioned prior to March 7, 1938, but ever since said date has not been and is not now in office as Collector of Internal Revenue of the United States.

V.

On January 1, 1936, plaintiff was the owner of four hundred (400) shares of the capital stock of Honolulu Oil Corporation, a corporation organized under the laws of the State of Delaware, which shares had been purchased by plaintiff subsequent to March 1, 1913, for the amount of Six Thousand Six Hundred Thirty-three and 25/100 Dollars ($6633.25). On or about July 24, 1936, plaintiff purchased an additional one hundred (100) shares of said capital stock of said corporation for the amount of Two Thousand Eight Hundred Fifty-seven and 50/100 Dollars ($2857.50). During the calendar year 1936 plaintiff received from said corporation cash distributions on said shares of stock in the sum of Four Hundred Fifty Dollars ($450.00). Plaintiff reported on his said income tax return for the calendar year 1936, on line 6 of said return, as taxable dividends received during the calendar year 1936, the total sum of One Thousand Seven Hundred Dollars ($1700.00), which said total sum included the aforementioned sum of Four Hundred Fifty Dollars ($450.00) received from said Honolulu Oil Corporation.

VI.

On or about June 12, 1939, plaintiff filed with the [3] Collector of Internal Revenue of the United States for the First District of California at San Francisco, California, a claim for refund of income taxes illegally collected from plaintiff for the calendar year 1936 in the sum of One Hundred Twenty-four and 84/100 Dollars ($124.84). Said claim for refund was based on the ground that plaintiff had sustained a deductible loss in the amount of One Thousand Dollars ($1000.00) during the calendar year 1936. A copy of said claim for refund of taxes illegally collected is attached hereto, marked Exhibit "A", and is hereby referred to and by such reference is made a part of this complaint as fully and to the same extent as if it were set out at large in this paragraph. Said claim, together with interest thereon in the amount of Twenty and 20/100 Dollars ($20.20), was allowed by said Commissioner of Internal Revenue by a Certificate of Overassessment issued in the month of March, 1940, and a portion thereof, to wit, the sum of One Hundred Thirty-two and 53/100 Dollars ($132.53), was repaid to plaintiff through a credit thereof to a deficiency in Federal income taxes owing by plaintiff for the calendar year 1937, and the balance thereof, to wit, the sum of Twelve and 51/100 Dollars ($12.51), was refunded to plaintiff on May 24, 1940.

VII.

On or about March 6, 1940, plaintiff filed with the Collector of Internal Revenue of the United States

for the First District of California at San Francisco, California, an amended claim for refund of income taxes illegally collected from plaintiff for the calendar year 1936 in the sum of One Hundred Seventy-six and 68/100 Dollars ($176.68), of which amount the sum of One Hundred Twenty-four and 84/100 Dollars ($124.84) represents that portion of said amended claim for [4] refund which was based on the grounds set forth in said original claim for refund filed on or about June 12, 1939, and which has been refunded to plaintiff as hereinabove in paragraph VI set forth. The balance of said amended claim for refund, to wit, the sum of Fifty-one and 84/100 Dollars ($51.84), was based on the ground that a portion, to wit, the sum of Four Hundred Thirty-two Dollars ($432.00), of the total cash distributions received by plaintiff during the calendar year 1936 from said Honolulu Oil Corporation was not paid out of the earnings or profits of said corporation accumulated after February 28, 1913, nor out of its earnings or profits for the taxable year 1936, in that said dividends were paid out of increase in value of property accrued before March 1, 1913, and that said portion was not subject to income tax in the hands of and was not taxable to plaintiff. A copy of said amended claim for refund of taxes illegally collected is hereto attached, marked Exhibit "B", and is hereby referred to and by such reference is made a part of this complaint as fully and to the same extent as if it were set out at large in this paragraph.

VIII.

Thereafter and on or about May 17, 1941, plaintiff filed with the Collector of Internal Revenue of the United States for the First District of California at San Francisco, California, a second amended claim for refund of income taxes illegally collected from plaintiff for the calendar year 1936 in the sum of One Hundred Seventy-six and 68/100 Dollars ($176.68), of which amount the sum of One Hundred Twenty-four and 84/100 Dollars ($124.84) represents that portion of said second amended claim for refund which was based on the grounds set forth in said original claim for refund filed on or about [5] June 12, 1939, and which has been refunded to plaintiff as hereinabove in paragraph VI set forth. The balance of said second amended claim for refund, to wit, the sum of Fifty-one and 84/100 Dollars ($51.84), was based on the ground that a portion, to wit, the sum of Four Hundred Thirty-two Dollars ($432.00), of the total cash distributions received by said plaintiff during the calendar year 1936 from said Honolulu Oil Corporation was not paid out of the earnings or profits of said corporation accumulated after February 28, 1913, nor out of its earnings or profits for the taxable year 1936, in that said dividends were paid out of increase in value of property accrued before March 1, 1913, and that said portion was not subject to income tax in the hands of and was not taxable to plaintiff. A copy of said second amended claim for refund of taxes illegally collected is hereto attached, marked Exhibit "C", and is hereby referred to and by such

reference is made a part of this complaint as fully and to the same extent as if it were set out at large in this paragraph.

IX.

On or about July 22, 1941, said amended claim for refund filed on or about March 6, 1940, was rejected and disallowed in full by said Commissioner of Internal Revenue, and no part of the amount claimed therein, other than the sum of One Hundred Twenty-four and 84/100 Dollars ($124.84), as hereinabove in paragraph VI set forth, has been credited, repaid or refunded. Notice of such rejection and disallowance was mailed to plaintiff by registered mail by said Commissioner on July 22, 1941.

X.

The action taken by said Commissioner of Internal [6] Revenue with respect to said second amended claim for refund filed on or about May 17, 1941, was and is as set forth in a letter dated February 10, 1942, addressed to plaintiff herein, and received by plaintiff on or about February 16, 1942. Said letter is in words and figures as follows:

"Treasury Department
Washington
Office of
Commissioner of Internal Revenue

Address Reply To Feb 10 1942
Commissioner of Internal Revenue
And Refer To
IT:C1:CC:3-EVL

Mr. L. A. Cranson,
215 Market Street,
San Francisco, California.

Sir:

Reference is made to Form 843 filed by you on May 17, 1941, with the Collector of Internal Revenue, San Francisco, California, requesting a refund of $176.68, income tax, for the year 1936. The Form 843 is considered an application for reconsideration of your claim for refund, which was disallowed, registered notice of disallowance having been mailed on July 22, 1941, in accordance with the provisions of the Internal Revenue laws.

The Bureau has considered the additional arguments presented in your Form 843, and in accordance with the findings of the Internal Revenue Agent in Charge, San Francisco, California, the disallowance of the above-mentioned claim is sustained.

In view of the foregoing, your application for reconsideration is denied.

Respectfully,

TIMOTHY C. MOONEY,
Deputy Commissioner,
By T. C. ATKESON,
Head of Division." [7]

XI.

Plaintiff alleges that only a portion of said cash distributions in the sum of Four Hundred Fifty Dollars ($450.00) received by plaintiff during the calendar year 1936 from said Honolulu Oil Corporation, to wit, the sum of not more than Eighteen Dollars ($18.00), was paid out of the earnings or profits of said corporation accumulated after February 28, 1913, or out of its earnings or profits for the taxable year 1936, and that the balance of said sum of Four Hundred Fifty Dollars ($450.00), to wit, an amount not less than the sum of Four Hundred Thirty-two Dollars ($432.00), was not paid out of the earnings or profits of said corporation accumulated after February 28, 1913, nor out of its earnings or profits for the taxable year 1936, and that said balance was not subject to income tax in the hands of and was not taxable to plaintiff. Plaintiff further alleges that he erroneously reported on his said income tax return for the calendar year 1936, as taxable dividends received from said Honolulu Oil Corporation, the total sum of Four Hundred Fifty Dollars ($450.00), whereas in truth and in fact a portion of said total sum, to wit,

not less than Four Hundred Thirty-two Dollars ($432.00), did not, nor did any part thereof, constitute a distribution out of the earnings or profits of said corporation accumulated after February 28, 1913, or out of its earnings or profits for the taxable year 1936, nor was said portion, nor any part thereof, subject to income tax, and plaintiff overpaid his income taxes for said calendar year in the sum of not less than Fifty-one and 84/100 Dollars ($51.84).

Wherefore, plaintiff prays judgment against the defendant herein for the sum of Fifty-one and 84/100 Dollars [8] ($51.84), together with interest thereon as by law provided, and for his cost in this behalf sustained.

MORRISON, HOHFELD, FOERSTER, SHUMAN & CLARK,
LEON de FREMERY,
Attorneys for Plaintiff. [9]

United States of America,
Northern District of California,
City and County of San Francisco.—ss.

Lorin A. Cranson, being first duly sworn, deposes and says:

He is the plaintiff named herein; he has read the foregoing Complaint to Recover Taxes Illegally Collected and knows the contents thereof; the same is true of his own knowledge, except as to the matters

which are therein stated on information or belief, and as to those matters he believes it to be true.

LORIN A. CRANSON,
L. A. CRANSON.
(Lorin A. Cranson)

Subscribed and sworn to before me this 10th day of April, 1942.

[Notarial Seal] HELEN G. BOYLE,
Notary Public in and for the City and County of San Francisco, State of California.
My Commission Expires Sept. 19, 1942. [10]

EXHIBIT "A"

Form 843
Treasury Department
Internal Revenue Service
(Revised April 1940)

CLAIM

To Be Filed With the Collector Where Assessment Was Made or Tax Paid

Collector's Stamp
(Date received)

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

[x] Refund of Tax Illegally Collected.

[ ] Refund of Amount Paid for Stamps Unused or Used in Error or Excess.

[ ] Abatement of Tax Assessed (not applicable to estate or income taxes).

State of California
City and County of San Francisco—ss:

Type or Print

Name of taxpayer or purchaser of stamps L. A. Cranson
Business address 215 Market Street, San Francisco, California
Residence .....

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed California
2. Period (if for income tax, make separate form for each taxable year) from January 1, 1936, to December 31, 1936
3. Character of assessment or tax Income
4. Amount of assessment, $1,166.86; dates of payment Statutory Dates
5. Date stamps were purchased from the Government .....
6. Amount to be refunded..... $124.84
7. Amount to be abated (not applicable to income or estate taxes) ..... $.....
8. The time within which this claim may be legally filed expires, under Section 322 of the Revenue Act of 1936, on March 15, 1940

The deponent verily believes that this claim should be allowed for the following reasons:

Your deponent hereby claims a loss sustained in

1936, not claimed on his original return, occasioned by investment in capital stock of Santa Clara Holding Company becoming worthless in 1936. The refund due is computed on Exhibit "A" attached hereto and made a part hereof.

My protest dated May 26, 1939, and filed with the Internal Revenue Agent in Charge at San Francisco, is made a part of this claim to the same extent as though the same had been fully incorporated herein.

(Attach letter-size sheets if space is not sufficient)

Signed L. A. CRANSON

Sworn to and subscribed before me this 2nd day of June 1939

[Seal] HELEN G. BOYLE

Notary Public in and for the City and County of San Francisco, State of California.

(See Instructions on Reverse Side)

[Printer's Note: Ruled forms on Reverse of sheet contain no entries.] [11]

L. A. CRANSON

CLAIM FOR REFUND OF OVERPAYMENT OF INCOME TAX

Statement attached to and made a part of Claim for Refund for Calendar Year 1936

Net Income per R. A. R. 3/24/38	$15,883.50
Less: Worthless stock of Santa Clara Holding Company	1,000.00
Revised Net Income	$14,883.50
Personal Exemption and Dependents	1,400.00
Surtax Net Income	$13,483.50
Earned Income Credit	1,400.00
Normal Tax Net Income	$12,083.50
Normal Tax	$ 483.34
Surtax	$ 558.68
Total Tax Assessable	$ 1,042.02
Tax Previously Assessed	$ 1,166.86
Refund being demanded	$ 124.84

[12]

EXHIBIT "B"

Form 843
Treasury Department
Internal Revenue Service
(Revised April 1940)

AMENDED CLAIM

To Be Filed With the Collector Where Assessment Was Made or Tax Paid

Collector's Stamp
(Date received)

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

[x] Refund of Tax Illegally Collected.

[ ] Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.

[ ] Abatement of Tax Assessed (not applicable to estate or income taxes).

State of California
City and County of San Francisco—ss:

Type or Print

Name of taxpayer or purchaser of stamps L. A. Cranson
Business address 215 Market Street, San Francisco, California
Residence .....

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed 1st California

2. Period (if for income tax, make separate form for each taxable year) from January 1, 1936, to December 31, 1936

3. Character of assessment or tax Income

4. Amount of assessment, $1,166.86; dates of payment Statutory dates

5. Date stamps were purchased from the Government .....

6. Amount to be refunded $176.68

7. Amount to be abated (not applicable to income or estate taxes) ..... $ .....

8. The time within which this claim may be legally filed expires, under Section 322 of the Revenue Act of 1936, on March 15, 1940

The deponent verily believes that this claim should be allowed for the following reasons:

See statement attached hereto and made a part hereof.

(Attach letter-size sheets if space is not sufficient)

Signed L. A. CRANSON

Sworn to and subscribed before me this 6th day of March 1940

[Seal] HELEN G. BOYLE,

Notary Public in and for the City and County of San Francisco, State of California

[Printer's Note: Ruled forms on Reverse of sheet contain no entries.] [13]

L. A. CRANSON

Statement Attached to and Made a Part of Amended Claim for Refund for the Calendar Year 1936

The deponent verily believes that this claim should be allowed for the following reasons:

Failure to deduct on returns filed, loss sustained in 1936 by reason of investment in capital stock of Santa Clara Holding Company becoming worthless in 1936. The original claim for refund and all the papers and documents attached thereto and referred to therein, are hereby made a part of this claim to the same extent as though attached hereto in full.

On my income tax return for the calendar year 1936, I reported as subject to tax, dividends from Honolulu Oil Corporation in the amount of $450.00. 96% of these dividends were paid out of increase in value of property accrued before March 1, 1913 and therefore $432.00 is exempt from tax. In computing the Corporation's earnings available for taxable dividends, it is necessary to take into account the following principal deductions:

1. Excess of depletion on March 1, 1913 value of the company's oil and gas properties over depletion sustained on cost of such properties.

2. All other items of unallowable deductions normally taken into account in the computation of earnings or profits available for taxable dividends, including losses upon dissolution during 1936 of wholly owned subsidiaries.

The refund due is computed as follows:

Net Income per R.A.R. 3/24/38	$15,883.50
Less: Dividends from Honolulu Oil Corporation paid out of increase in value of property accrued before 3/1/13	432.00
Worthless stock of Santa Clara Holding Co	1,000.00
Revised Net Income	$14,451.50
Personal Exemption and Dependents	1,400.00
Surtax Net Income	$13,051.50
Earned Income Credit	1,400.00
Normal Tax Net Income	$11,651.50
Normal Tax	$ 466.06
Surtax	524.12
Total Tax Assessable	$ 990.18
Tax Previously Assessed	1,166.86
Refund being demanded	$ 176.68

[14]

EXHIBIT "C"

Form 843
Treasury Department
Internal Revenue Service
(Revised April 1940)

SECOND AMENDED CLAIM

To Be Filed With the Collector Where Assessment Was Made or Tax Paid

Collector's Stamp
(Date received)

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

[x] Refund of Tax Illegally Collected.

[ ] Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.

[ ] Abatement of Tax Assessed (not applicable to estate or income taxes).

State of California
City and County of San Francisco—ss:

Type or Print
Name of taxpayer or
purchaser of stamps Lorin A. Cranson
Business address 215 Market Street,
San Francisco, California
Residence .....

The deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed 1st California

2. Period (if for income tax, make separate form for each taxable year) from January 1, 1936, to December 31, 1936

3. Character of assessment or tax Income

4. Amount of assessment, $1,166.86; dates of payment statutory dates

5. Date stamps were purchased from the Government .....

6. Amount to be refunded $176.68

7. Amount to be abated (not applicable to income or estate taxes) ..... $ .....

8. The time within which this claim may be legally filed expires, under Section 322 of the Revenue Act of 1936, on March 15, 1940

The deponent verily believes that this claim should be allowed for the following reasons:

See statement attached hereto and made a part hereof.

(Attach letter-size sheets if space is not sufficient)

Signed LORIN A. CRANSON

Sworn to and subscribed before me this 14th day of May 1941

[Seal] HELEN G. BOYLE,

Notary Public in and for the City and County of San Francisco, State of California

[Printer's Note: Ruled forms on Reverse of sheet contain no entries.] [15]

LORIN A. CRANSON

Statement Attached to and Made a Part of Second Amended Claim for Refund for the Calendar Year 1936

The deponent verily believes that this claim should be allowed for the following reasons:

Failure to deduct on returns filed, loss sustained in 1936 by reason of investment in capital stock of Santa Clara Holding Company becoming worthless in 1936. The original claim for refund and all the papers and documents attached thereto and referred to therein, are hereby made a part of this claim to the same extent as though attached hereto in full.

On my income tax return for the calendar year 1936, I reported as subject to tax, dividends from Honolulu Oil Corporation in the amount of $450.00. 96% of these dividends were paid out of increase in value of property accrued before March 1, 1913 and therefore $432.00 is exempt from tax. In computing the Corporation's earnings available for taxable dividends, it is necessary to take into account the following principal deductions:

1. Excess of depletion on March 1, 1913 value of the company's oil and gas properties over depletion sustained on cost of such properties.

2. All other items of unallowable deductions normally taken into account in the computation of earnings or profits available for taxable dividends, including losses upon dissolution during 1936 of wholly owned subsidiaries.

3. In the event it should be held that losses upon dissolution during 1936 of wholly owned subsidiaries do not reduce earnings or profits of Honolulu Oil Corporation available for dividends, it is then contended in the alternative that the operating deficits of the subsidiary corporations existing as of the date of their dissolution were absorbed by Honolulu Oil Corporation and had the effect of reducing the earnings or profits of Honolulu Oil Corporation available for dividends.

The refund due is computed as follows:

Net Income per R.A.R. 3/24/38	$15,883.50
Less: Dividends from Honolulu Oil Corporation paid out of increase in value of property accrued before 3/1/13	432.00
Worthless stock of Santa Clara Holding Co.	1,000.00
Revised Net Income	$14,451.50
Personal Exemption and Dependents	1,400.00
Surtax Net Income	$13,051.50
Earned Income Credit	1,400.00
Normal Tax Net Income	$11,651.50
Normal Tax	466.06
Surtax	524.12
Total Tax Assessable	$ 990.18
Tax Previously Assessed	1,166.86
Refund being demanded	$ 176.68

[Endorsed]: Filed April 22, 1942. [16]

[Title of District Court and Cause.]

ANSWER

Comes now the above-named defendant through his duly appointed attorney, Frank J. Hennessy, Esquire, United States Attorney for the Northern District of California, and answers the complaint filed herein as follows:

I.

Admits the allegations of fact contained in paragraph I of plaintiff's complaint.

II.

Admits the allegations of fact contained in paragraph II of plaintiff's complaint except it is denied that the income tax return was filed on March 15, 1937 but admits that said return was filed on March 13, 1937; denies the payment of $254.35 alleged to be made on March 15, 1937 but admits payment of $254.35 on March 13, 1937; denies the payment of the sum of $254.35 on June 15, 1937 but admits the payment of $254.35 on June 14, 1937; denies payment of $254.34 on September 15, 1937 but admits the payment of $254.34 on September 8, 1937.

III.

Admits the allegations of fact contained in paragraph III of plaintiff's complaint except it is denied that the sum of $149.48 was paid on March 21, 1938 but admits that the sum of $149.48 was paid March 25, 1938; [18] denies payment of interest in the sum of $9.21 on April 15, 1938 but admits payment of interest in the amount of $9.21 on April 18, 1938.

IV.

Admits the allegations of fact contained in paragraph IV of plaintiff's complaint.

V.

For lack of knowledge and information sufficient to form a belief defendant denies the allegations of fact set forth in paragraph V of plaintiff's complaint except it is admitted that plaintiff reported on his income tax return for the calendar year 1936 on line 6 of said return as taxable dividends received during the calendar 1936 the total sum of $1,700.00.

VI.

Admits the allegations of fact contained in paragraph VI of plaintiff's complaint except it is denied that the claim for refund was filed on June 12, 1938 but admits that it was filed on June 13, 1939.

VII.

Denies the allegations of fact contained in paragraph VII of plaintiff's complaint except it is admitted that claim for refund in the sum of $176.68 was filed on March 7, 1940, of which amount the sum of $124.84 represents that portion of said amended claim for refund which was based on the grounds set forth in said original claim for refund filed on June 13, 1939, and which has been refunded to the plaintiff. Defendant admits that plaintiff's claim for refund attached to its complaint as Exhibit "B" is a true and correct copy of the claim for refund filed with the Collector of Internal Reve-

nue and that such claim speaks for itself as such, and further admits no part of the facts set forth in said claim for refund. [19]

VIII.

Admits that the second amended claim for refund was filed on May 17, 1941 in the sum of $176.68, of which amount the sum of $124.84 represents that portion of said second amended claim for refund which was based on the grounds set forth in said original claim for refund filed on June 13, 1939, and which has been refunded to plaintiff. Otherwise, denies the allegations of fact contained in paragraph VIII of plaintiff's complaint except defendant admits that plaintiff's claim for refund attached to its complaint as Exhibit "C" is a true and correct copy of the claim for refund filed with the Collector of Internal Revenue and that such claim speaks for itself as such, and further admits no part of the facts set forth in said claim for refund.

IX.

Admits the allegations of fact contained in paragraph IX of plaintiff's complaint.

X.

Admits the allegations of fact contained in paragraph X of plaintiff's complaint.

XI.

Denies the allegations or purported allegations of fact contained in paragraph XI of plaintiff's complaint.

Wherefore, having fully answered the complaint filed herein, defendant respectfully prays that plaintiff's complaint be dismissed and judgment be entered in his favor for costs and such other appropriate relief as he may be entitled to under the law.

FRANK J. HENNESSY,
United States Attorney,
Attorney for Defendant.
By W. E. LECKING,
Asst. U. S. Atty.

(Receipt of Service.)

[Endorsed]: Filed July 11, 1942. [20]

[Title of District Court and Cause.]

STIPULATION

It Is Hereby Stipulated and Agreed by and between the parties hereto, by their respective attorneys, that the following facts shall be taken as true upon the trial of the above-entitled case, provided, however, that this stipulation shall be without [21] prejudice to the right of either party to introduce other and further evidence not inconsistent with the facts herein stipulated to be taken as true.

1. At all times herein mentioned plaintiff was a resident of San Francisco, California, and of the judicial district described as the Northern District of California, Southern Division. Plaintiff is the sole and absolute owner of the claim sued on herein, and is the sole person interested therein, and no

assignment or transfer of said claim, or of any part thereof or interest therein, has been made by plaintiff. No action other than that set forth in the complaint has been taken in Congress or by any of the Departments. Plaintiff has at all times borne true allegiance to the Government of the United States, and has not in any way aided, abetted or given encouragement to rebellion against said Government.

2. On March 13, 1937, plaintiff filed with the Collector of Internal Revenue of the United States for the First District of California an individual income tax return for the calendar year 1936, disclosing a net income of $14,683.50 and a total tax due of $1,017.38, which amount was duly assessed and was paid in quarterly installments during the year 1937 to John V. Lewis, as said Collector of Internal Revenue. Said John V. Lewis ever since March 7, 1938, has not been and is not now in office as Collector of Internal Revenue of the United States. A copy of said return is hereunto attached, marked Exhibit "A", and made a part hereof.

3. On January 1, 1936, plaintiff was the owner of 400 shares of the capital stock of Honolulu Oil Corporation, Ltd., and on July 24, 1936, plaintiff purchased an additional 100 shares of the capital stock of said corporation. The basis on January 1, [22] 1936, for income tax purposes of each of said shares of stock was greater than the aggregate cash distributions paid by said corporation during said year on each of said shares. During the calendar year 1936 plaintiff received from said corporation cash

distributions on said shares of stock in the sum of $450, which plaintiff reported as taxable dividends received on his said income tax return for the calendar year 1936.

4. On March 24, 1938, the Internal Revenue Agent in Charge at San Francisco addressed a letter to the plaintiff enclosing a copy of report covering his examination of plaintiff's books and records, and disclosing a deficiency in tax of $149.48 for 1936. Said deficiency, plus interest of $9.21, was duly assessed and was paid in two installments on March 25 and April 18, 1938. A copy of said letter is hereunto attached, marked Exhibit "B", and made a part hereof.

5. By a Certificate of Overassessment, No. 2534937, issued in or about March, 1940, plaintiff was advised of an overassessment of tax for the year 1936 in the amount of $124.84, plus interest thereon in the amount of $7.69, which resulted from the allowance of plaintiff's original claim for refund (Exhibit "A" of plaintiff's complaint). This amount was allowed on Schedule No. 70750, and was thereafter duly paid to plaintiff. A copy of said certificate is hereunto attached, marked Exhibit "C", and made a part hereof.

6. On March 7, 1940, plaintiff filed with the Collector of Internal Revenue of the United States for the First District of California an amended claim for refund of income taxes paid for the calendar year 1936. Disregarding items not now material, a portion of said claim, amounting to $51.84, was based on the ground that only $18 out of the $450

received as distributions by plaintiff during the [23] calendar year 1936 from Honolulu Oil Corporation, Ltd., were taxable dividends, and that the balance of said distributions, namely, the sum of $432, was not paid out of the earnings or profits of said corporation accumulated after February 28, 1913, nor out of its earnings or profits for the taxable year 1936, and was not taxable to plaintiff. A copy of said amended claim for refund is hereunto attached, marked Exhibit "D", and made a part hereof.

7. On May 14, 1941, the Internal Revenue Agent in Charge at San Francisco, California, addressed a letter to plaintiff regarding the aforesaid amended claim filed March 7, 1940, and by letter dated July 22, 1941, the Commissioner of Internal Revenue advised plaintiff that that claim was rejected. Copies of said letters dated May 14 and July 22, 1941, are hereto attached, marked Exhibit "E", and made a part hereof.

8. On May 17, 1941, plaintiff filed with the aforesaid Collector of Internal Revenue a second amended claim for refund of income taxes paid for the calendar year 1936. Disregarding items not now material, a portion of said claim, amounting to $51.84, was likewise based on the ground that only $18 out of the $450 received as distributions by plaintiff during the calendar year 1936 from Honolulu Oil Corporation, Ltd., were taxable dividends, and that the balance of said distributions, namely, the sum of $432, was not paid out of the earnings or profits of said corporation accumulated after Feb-

ruary 28, 1913, nor out of its earnings or profits for the taxable year 1936, and was not taxable to plaintiff. A copy of said second amended claim for refund is hereunto attached, marked Exhibit "F", and made a part hereof.

9. On February 10, 1942, the Commissioner of Internal Revenue addressed a letter to plaintiff regarding the aforesaid second amended claim filed May 17, 1941. A copy of said letter is hereunto attached, marked Exhibit "G", and made a part hereof. [24]

10. Honolulu Consolidated Oil Company was incorporated in 1910 under the laws of the State of California, and in 1930 said corporation was reincorporated under the laws of the State of Delaware as Honolulu Oil Corporation, Ltd., at which time the shareholders of Honolulu Consolidated Oil Company exchanged their stock for stock of Honolulu Oil Corporation, Ltd., on a share for share basis. On May 26, 1937, the name of the corporation was changed to Honolulu Oil Corporation. Both of said corporations are hereinafter referred to as "Honolulu".

11. California Exploration Company was incorporated on June 27, 1927, under the laws of the State of Nevada. The primary business of said corporation was the acquisition and development of prospective oil properties in the State of Wyoming. Honolulu Oil Company was incorporated on November 2, 1929, under the laws of the State of Nevada. The primary business of said corporation was the acquisition and development of prospective

oil properties in the State of Texas. On August 4, 1934, said corporations were consolidated under the name of California Exploration Company, which name was thereupon changed to California Exploration Company, Inc. The assets of each of said constituent corporations were carried on the books of said corporations at cost, and the reserves for depreciation and depletion of each of said corporations, as shown by the books of each of said corporations, were computed on said cost. The assets, liabilities and reserves of each of said constituent corporations, as shown by its books, were carried forward in the same amounts on the books of the consolidated company, California Exploration Company, Inc.

12. Sea Cliff Development Company, Ltd., was incorporated on February 17, 1930, under the laws of the State of Nevada. [25] The primary business of said corporation was the acquisition and development of prospective oil properties in the Rincon Oil Field, Ventura County, California.

13. Petroleum Hydrogenation Company, Ltd., was incorporated on August 9, 1930, under the laws of the State of Nevada, and on November 25, 1930, its name was changed to Processco, Limited. Said corporation was formed primarily to acquire and develop patents relating to the processing of crude petroleum.

14. The aforesaid California Exploration Company, Inc., Sea Cliff Development Company, Ltd., and Processco, Limited, are hereinafter collectively referred to as "Subsidiaries". At all times since

their incorporation Honolulu owned all the issued and outstanding capital stock of said Subsidiaries, and likewise at all times since the incorporation of the predecessors of California Exploration Company, Inc., Honolulu owned all the issued and outstanding capital stock of said predecessors. On August 31, 1936, the said Subsidiaries were liquidated, and distributed to their sole stockholder, Honolulu, all their assets, subject to their liabilities, in complete cancellation and redemption of all their issued and outstanding capital stock, and said Subsidiaries ceased to transact business and dissolved. Upon the liquidation of said Subsidiaries, Honolulu realized a loss of $1,225,908.63, which was the amount charged off on its books as a loss, no portion of which was recognized for Federal income tax purposes under the provisions of section 112(b)(6) of the Revenue Act of 1936, and was so treated by Honolulu in its 1936 Federal income and excess-profits tax return. Said loss of $1,225,908.63 was computed as follows: [26]

Cash invested by Honolulu in the capital stock of said Subsidiaries, including the predecessors of California Exploration Company, Inc.:		
California Exploration Company	$ 470,000.00	
Honolulu Oil Company	198,000.00	
Total cost of stock of predecessors of California Exploration Company, Inc.	$ 668,000.00	
Additional investment in stock of California Exploration Company, Inc.	470,000.00	
Total cost of stock of California Exploration Company, Inc.	$ 1,138,000.00	
Sea Cliff Development Company, Ltd.	345,000.00	
Processco, Limited	100,000.00	$ 1,583,000.00
Cash advances by Honolulu to said Subsidiaries remaining unpaid at date of liquidation:		
California Exploration Company, Inc.	$ 31.54	
Sea Cliff Development Company, Ltd.	3,082.77	
Processco, Limited	84,051.93	87,166.24
Paid by Honolulu to third parties for their contingent interest in capital stock of Processco, Limited, under a contract under which said parties would become entitled to certain shares of stock if the net profits of said corporation should exceed 6 per cent of its average invested capital for twelve successive calendar months		20,457.02
Total investment and advances by Honolulu		$ 1,690,623.26

Less assets acquired from said Subsidiaries (minus liabilities assumed) per Exhibit "H" attached hereto and made a part hereof	464,714.63
Loss charged off by Honolulu on its books upon liquidation of said Subsidiaries	$ 1,225,908.63

The assets acquired by Honolulu upon the liquidation of [27] said subsidiaries were carried on the books of said Subsidiaries at the cost to said Subsidiaries (or in the case of assets originally acquired by the predecessors of California Exploration Company, Inc., at the cost to said predecessors). The accounts representing said assets on the books of said Subsidiaries, together with reserves for depreciation and depletion computed on said cost, a reserve for bad debts, and the accounts representing the liabilities assumed by Honolulu, were transferred without change to the books of Honolulu. The total of said assets, less said liabilities and reserves, transferred to the books of Honolulu amounted to the sum of $464,714.63, as above set forth. The aggregate value of said assets, less said liabilities and reserves, did not exceed said sum of $464,714.63, and for the purposes of this stipulation it is agreed that their aggregate value, less said liabilities and reserves, is the sum of $464,-714.63. For the purpose of determining earnings or profits available for dividends after August 31, 1936, Honolulu used the cost of said assets, as above set forth, in the determination of depreciation, depletion, and gain or loss on the sale or other disposition thereof.

15. The surplus of Honolulu as of March 1, 1913, is allocated as follows:

Earned surplus	$ 426,918.44
Paid-in surplus	$ 2,501,673.44
Surplus by appreciation	$15,226,408.55

16. During the years 1913 to 1935, inclusive, Honolulu paid the following dividends from March 1, 1913 surplus and appreciation existing on March 1, 1913:

Year	Amount
1914	$ 93,191.16
1915	235,876.98
1916	105,583.93
1917	360,000.00
1918	7,155.11
Total	$801,807.18

[28]

17. The predecessors of California Exploration Company, Inc., sustained operating losses during the period from their incorporation to their consolidation, as follows:

California Exploration Company	$427,909.64
Honolulu Oil Company	325,322.64
Total operating deficit carried onto the books of the consolidated company, California Exploration Company, Inc.	$753,232.28

Each of said Subsidiaries sustained operating losses during the period from their incorporation to their dissolution, and the resulting operating deficits of said Subsidiaries as of the date of their liquidation on August 31, 1936, were as follows:

California Exploration Company, Inc.:	
Acquired from predecessors as above set forth	$753,232.28
Resulting from operating losses subsequent to consolidation	194,795.44
Sea Cliff Development Company, Ltd.	156,278.11
Processco, Limited	101,145.78
Total operating deficits of Subsidiaries	$1,205,451.61

18. For the years 1928 to 1933, inclusive, Honolulu filed consolidated returns, and the operating losses of these Subsidiaries were applied for income tax purposes in reduction of the net income of Honolulu as follows (Honolulu acquired the stock of the Sea Cliff Development Company in December, 1933):

Year	California Exploration Company	Honolulu Oil Company	Processco Limited	Total Loss for Year
1928	$152,741.96	$	$	$152,741.96
1929	91,929.50	.....	.....	91,929.50
1930	98,324.77	93,909.60	2,097.24	194,331.61
1931	25,387.28	115,178,56	5,491.57	146,057.41
1932	15,850.83	74,330.13	18,909.71	109,090.67
1933	15,645.50	53,515.04	5,791.98	74,952.52
Total	$399,879.84	$336,933.33	$ 32,290.50	$769,103.67

[29]

The taxable net income of Honolulu after reduction of operating losses of the subsidiary companies is shown as follows:

Year	Amount
1928	$ 1,364,334.08
1929	1,433,602.91
1930	1,553,754.99
1931	123,151.83
1932	547,582.01
1933 (loss)	(243,578.74)

As all of the aforesaid companies had operating losses for the year 1933, the operating losses of the three subsidiary companies availed of in the consolidated returns covering the years 1928 to 1932, inclusive, amounted to $694,151.15 ($769,-103.67 less $74,952.52).

19. At all times during the calendar year 1936 Honolulu had outstanding 937,743 shares of capital stock, on which it paid four cash distributions of twenty-five cents per share each on March 14, June 15, September 15, and December 15. On January 1, 1936, Honolulu had available for dividends earnings or profits accumulated since February 28, 1913, in the amount of $139,631.26. Honolulu's earnings or profits during the calendar year 1936 amounted to the sum of $931,553.82 before deducting any portion of said loss realized upon the liquidation of said Subsidiaries on August 31, 1936, in the amount of $1,225,908.63, or before deducting the aggregate operating deficits of said subsidiaries in the amount of $1,205,451.61.

Dated: Feb. 4th, 1943.

MORRISON, HOHFELD, FOERSTER, SHUMAN & CLARK,
LEON de FREMERY,
Attorneys for Plaintiff.
FRANK J. HENNESSY,
Attorney for Defendant. [30]

EXHIBIT A

Return Form Marked "Duplicate" Must Be Filed With This Original Return

Form 1040
Treasury Department
Internal Revenue
Service

(Auditor's Stamp)

INDIVIDUAL INCOME TAX RETURN

For Net Incomes From Salaries or Wages of More Than $5,000 and Incomes From Business, Profession, Rents, or Sale of Porperty.

FOR CALENDAR YEAR 1936

or fiscal year begun.....,1936, and ended ....., 1937

File This Return Not Later Than the 15th Day of the Third Month Following the Close of the Taxable Year.

Print Name and Address Plainly Below
(See Instruction 28)

LORIN A. CRANSON
(Name) (Both husband and wife, if this is a joint return)

215 Market Street
(Street and number, or rural route)

San Francisco (Post office) San Francisco (County) California (State)

Do Note Write in These Spaces

File Code

Serial Number

District

(Cashier's Stamp)

Cash Check M.O.
Cert. of Ind.

First Payment

$.....

Exhibit A—(Continued)

1. State whether you are (a) a citizen of the United States, or (b) a resident alien—Citizen.

2. If you filed a return for the preceding year, to which Collector's office was it sent?—S. F.

3. Were you married and living with husband or wife during your taxable year?—No.

4. Is this a joint return of husband and wife (see Instruction 21)?—No.

5. State name of husband or wife if a separate return was made and the Collector's office to which it was sent—XX

6. If not married, were you the head of a family (see Instruction 22 for definition) during your taxable year?—No.

7. How many dependent persons (other than husband or wife) under 18 years of age or incapable of self-support received their chief support from you during your taxable year?—One.

8. If your status in respect to question 3, 6, or 7 changed during the year, state date and nature of change—None.

9. State whether your books are kept on cash or accrual basis.....

10. State principal occupation or profession accounting for salaries, wages, commissions, fees, etc., in Item 1—Corporation Executive.

11. Did you transfer to or receive from any one person money or property in excess of $5,000, during the calendar year 1936, without an adequate and full consideration in money or money's worth?—No.
(Answer "yes" or "no")

If, so, did you file a gift tax return on Form 709 or an information return on Form 710?—No..
(Answer "yes" or "no")

12. Did any person or persons advise you in respect of any question or matter affecting any item or schedule of this return, or assist or ad-

Exhibit A—(Continued)

12. (Continued)

vise you in the preparation of this return, or actually prepare this return for you?—No.
(Answer "yes" or "no")

If so, give the name and address of such person or persons and state the nature and extent of the assistance or advice received by you and the items or schedules in respect of which the assistance or advice was received; if this return was actually prepared by any person or persons other than yourself, state the source of the information reported in this return and the manner in which it was furnished to or obtained by such person or persons.....

13. Did you make a return of information on Forms 1096 and 1099 (see Instruction 31) for the calendar year 1936? (Answer "yes" or "no")—No.

Attach Remittance Here

Item and Instruction No.	INCOME	Amount received	Expenses paid (Explain in Schedule F)	
1.	Salaries, Wages, Commissions, Fees, et. (State names and address of employer)			
	Honolulu Oil Corporation, Ltd..... 215 Market Street, San Francisco.....	$.....	$.....	$14,160.00 .....
2.	Net Profit (or Loss) from Business or Profession. (From Schedule A).... (State kind of business)			.....
3.	Interest on Bank Deposits, Notes, Corporation Bonds, etc. (except interest on tax-free covenant bonds). (Attach detailed statement).....			421.50
4.	Interest on Tax-free Covenant Bonds Upon Which a Tax was Paid at Source. (Attach detailed statement)			.....
5.	Taxable Interest on Government obligations, etc. (From Schedule D, Line (g))			.....
6.	Dividends. (From Schedule E)			1,700.00

Exhibit A—(Continued)

Item and Instruction No.	INCOME—(Continued)		
7.	Income (or Loss) from Partnerships, Syndicates, Pools, etc. (Furnish name, address, and kind of business)	.....	
8.	Income from Fiduciaries. (Furnish name and address)	.....	
9.	Rents and Royalties. (From Schedule B)	.....	
10.	Capital Gain (or Loss). (From Schedule C) (If capital loss, this amount may not exceed $2,000)	.....	
11.	Other Income. (State nature.) (Use separate schedule, if necessary)	.....	
12.	Total Income in Items 1 to 11		$16,281.50
	DEDUCTIONS		
13.	Interest paid. (Explain in Schedule F)	$ 68.59	
14.	Taxes Paid. (Explain in Schedule F)	261.41	
15.	Losses by Fire, Storm, etc. (Explain in table at foot of page 2)	.....	
16.	Bad Debts (including bonds determined to be worthless during taxable year). (Explain in Schedule F)	.....	
17.	Contributions. (Explain in Schedule F)	68.00	
18.	Other Deductions Authorized by Law (including stock determined to be worthless during taxable year). (Explain in Schedule F)	1,200.00	
19.	Total Deductions in Items 13 to 18		1,598.00
20.	Net Income (Item 12 minus Item 19)		$14,683.50

Exhibit A—(Continued)

COMPUTATION OF TAX (See Instruction 23)

Item and Instruction No.			
21.	Net income (Item 20 above)		$14,683.50
22.	Less: Personal exemption	$1,000.00	
23.	Credit for Dependents. (Explain in Schedule F)	400.00	1,400.00
24.	Balance (Surtax net income)		$13,283.50
25.	Less: Interest on Government obligations, etc. (Item 5)	$	
26.	Earned income credit. (See Instruction 22)		1,416.00
27.	Balance subject to normal tax		$11,867.50
28.	Normal tax (4% of Item 27)		$ 474.70
29.	Surtax on Item 24. (See Instruction 23)		542.68
30.	Total tax. (Item 28 plus Item 29)		$ 1,017.38
31.	Less: Income tax paid at source (2% of item 4)	$	
32.	Income tax paid to a foreign country or U. S. possession		
33.	Balance of Tax. (Item 30 minus Items 31 and 32)		$ 1,017.38

Exhibit A—(Continued)

AFFIDAVIT (See Instruction 27)

I/we swear (or affirm) that this return (including its accompanying schedules and statements, if any) has been examined by me/us, and to the best of my/our knowledge and belief is a true, correct, and complete return, made in good faith, for the taxable year stated, pursuant to the Revenue Act of 1936 and the Regulations issued thereunder.

Subscribed and sworn to by.....
before me this.....day of....., 193....

.....
(Signature and title of officer administering oath)

[Notarial Seal]

.....
(Signature) (See Instruction 27)

.....
(Signature)

A Return Made by an Agent Must Be Accompanied by Power of Attorney (See Instr. 27)

Exhibit A—(Continued)

AFFIDAVIT (See Instruction 27)

I/we swear (or affirm) that I/we prepared this return for the person or persons named herein and that the return (including its accompanying schedules and statements, if any) is a true, correct, and complete statement of all the information respecting the income tax liability of the person or persons for whom this return has been prepared of which I/we have any knowledge.

Subscribed and sworn to be fore me this..... day of....., 193....

.....
(Signature of person preparing the return)

.....
(Signature of officer administering oath) (Title)

.....
(Signature of person preparing the return)

[Notarial Seal]

.....
(Name of firm or employer, if any)

[31]

SCHEDULE A—PROFIT (OR LOSS) FROM BUSINESS OR PROFESSION (See Instruction 2)

[Printer's Note]: Followed by printed form not filled in.

SCHEDULE B—INCOME FROM RENTS AND ROYALTIES (See Instruction 9)

[Printer's Note]: Followed by printed form not filled in.

Exhibit A—(Continued)

SCHEDULE C—CAPITAL GAINS AND LOSSES (From Sales or Exchanges Only)
(See Instruction 10)

[Printer's Note]: Followed by printed form not filled in.

SCHEDULE D—INTEREST ON GOVERNMENT OBLIGATIONS, ETC. (See Instruction 5)

[Printer's Note]: Followed by printed form not filled in.

SCHEDULE E—INCOME FROM DIVIDENDS

Itemize all dividends received during the year, stating amounts and names and addresses of corporations declaring the dividends:

Honolulu Oil Corporation, Ltd., 215 Market St., San Francisco, California	450.00
Western States Gasoline Corporation, 609 So. Grand Ave., Los Angeles, California	1,250.00

Exhibit A—(Continued)

SCHEDULE F—EXPLANATION OF DEDUCTIONS CLAIMED IN ITEMS 1, 13, 14, 16, 17, AND 18, AND CREDIT CLAIMED IN ITEM 23

Interest, Sprig Farm Assn.	37.65)	Dues Tax, Sp. Farm Assn.	29.50
Interest, American Trust Co.	30.94)	Lake County Taxes	7.09
Club dues, Olympic Club (Tax)	8.84	Tiny Buck Club	12.00
Deposit box rent	.60	Community Chest	50.00
State Income Tax	211.01	Childrens' Theatre	5.00
S. F. City & County	4.37	T. B. Stamps	1.00

[Slip of paper pasted on form]

Support of niece under 18 years of age, Barbara McHugh	400.00
Worthless stock, 120 shares of Oilfields Electrical Engineering Corporation, Ltd.	1,200.00

EXPLANATION FOR DEDUCTION FOR LOSSES BY FIRE, STORM, ETC., CLAIMED IN SCHEDULE A AND IN ITEM 15

[Printer's Note]: Followed by printed form not filled in.

EXHIBIT B

Treasury Department
Internal Revenue Service
433 Federal Office Building
San Francisco, Calif.

Office of
Internal Revenue Agent in Charge
San Francisco Division
Lorin A. Cranson,
215 Market Street,
San Francisco, California.

In re: Income Tax
Date of Report: Mar 24 1938
Year Examined: 1936

Enclosed herewith you will find copy of report covering examination recently made by a representative of this office, concerning your income tax liability, which is furnished for your information and files.

Kindly acknowledge receipt of the enclosed report to the undersigned by return mail.

Respectfully,
F. M. HARLESS,
Internal Revenue Agent in Charge.

Enclosures:
Form 892-SF
hgk [32]

Preliminary Statement
Year 1936

Taxpayer: Lorin A. Cranson

Examining Officer: Bernard Cytron

Table of Contents

Schedule No. 1 Block Adjustments
1A Explanation of Items
2 Computation of Tax

Principal causes of additional tax: Disallowance of loss on worthless stock. All changes were discussed with Lorin A. Cranson who agrees to the adjustments. Status and reason for exemption: Single—Chief support of niece under 18 years of age.

SCHEDULE No. 1—Year 1936

Block Adjustments

	Return	Additions to Income	Corrected
1. Salary	$14,160.00		$14,160.00
3. Interest	421.50		421.50
6. Dividends	1,700.00		1,700.00
12. Total Income	$16,281.50		$16,281.50
13. Interest	68.59		68.59
14. Taxes	261.41		261.41
17. Contributions	68.00		68.00
18. Other deductions	1,200.00	$ 1,200.00	
19. Total deductions	$ 1,598.00		$ 398.00
20. Net Income	$14,683.50	$ 1,200.00	$15,883.50

SCHEDULE No. 1-A—Year 1936

Explanation of Items

Line 18.	Other deductions claimed	$ 1,200.00
	Other deductions allowed	—0—
	Increase in income	$ 1,200.00

Increase is due to disallowance of loss on worthless stock. The charter of the Oilfields Electrical Engineering Corporation, a California corporation, was forfeited in 1932 when the corporation failed to pay its franchise tax, and the stock became worthless prior to 1936.

SCHEDULE No. 2—Year 1936

Computation of Tax

1.	Net income (from Schedule 1)		$15,883.50
2.	Less: Personal exemption	$1,000.00	
3.	Credit for dependents	400.00	1,400.00
4.	Balance (surtax net income		$14,483.50
6.	Less: Earned income credit		1,400.00
7.	Balance subject to normal tax		$13,083.50
8.	Normal tax at 4 percent	523.34	
9.	Surtax	643.52	
13.	Total tax assessable		$ 1,166.86
14.	Tax previously assessed		$ 1,017.38
15.	Additional tax to be assessed		$ 149.48

EXHIBIT C

Treasury Department
Office of
Commissioner of Internal Revenue
Washington

Income Tax Unit
IT:C1:CC

Certificate of
Overassment
Number: 2534937
Allowed: $132.53
Schedule No. 70750

Mr. Lorin A. Cranson,
c/o C. Wm. Wittman, Jr.,
215 Market Street,
San Francisco, California.

Sir:

An audit of your income tax return, form 1040, and a consideration of all the claims (if any) filed by you for the taxable year ended December 31, 1936 indicates that the tax assessed for that year was in excess of the amount due:

Tax Assessed:	Income Tax	Interest
Original, account #201858	$1,017.38	None
Additional, March 1938 list, #510348	149.48	$9.21
Total assessed	$1,166.86	$9.21
Correct liability	1,042.02	1.52
Overassessment	$ 124.84	$7.69

This overassessment is in accordance with adjustments to your tax liability to which you have agreed.

The amount of the overassessment will be abated, credited, or refunded as indicated below. (You will be relieved from the payment of any amount abated; if an overpayment has been made and other taxes are due, credit will be made accordingly, and any amount refundable is covered by a Treasury check transmitted herewith.)

Included in the accompanying check is interest in the amount stated below, allowed on the refund or credit.

By direction of the Deputy Commissioner:

Respectfully,

T. C. ATKESON

Head of Division.

Abated: $

Credited: $132.53

To Tax. Year 1937

1940-Mar-1-519007

Credited: $

To Tax. Year

Refunded: $

Interest: $12.51

[Typed in Margin]: Note:—The interest, if any, included herein is taxable income, and must be included in your income tax return for the year in which received. [34]

EXHIBIT D

[Printer's Note: Exhibit "D" is not reproduced here as it is identical with Exhibit "B", the Amended Claim attached to the complaint, and set out in full at page 16 of this printed record.] [35-36]

EXHIBIT E

Treasury Department
Internal Revenue Service
74 New Montgomery Street
San Francisco, California

Office of
Internal Revenue Agent in Charge
San Francisco Division

May 14, 1941

Mr. Lorin A. Cranson,
215 Market Street,
San Francisco, California.

Sir:

I enclose a copy of the report of the examination of your income tax returns for the years ending December 31, 1936, in connection with your claim for a refund of $176.68. The report, which has been carefully reviewed by this office, discloses no ground for reduction of your tax liability.

If You Agree to the conclusions expressed in the report, please so advise this office at your earliest convenience.

If You Do Not Agree to these conclusions, you may file a protest, executed in triplicate under oath, with this office, within 30 days from the date of this letter, stating the grounds for your exceptions. Any protest so filed will have careful consideration and, if you so request, an opportunity for a hearing in this office will be granted you. This office will be pleased to answer any questions which may occur

to you in your examination of the enclosed copy of the report.

Should you fail to file with this office within the 30-day period mentioned either an acceptance of the conclusions expressed in the report or a written protest, a recommendation will be made to the Commissioner of Internal Revenue that your claim be disallowed.

Your prompt acknowledgment of the receipt of this letter and related papers upon the enclosed form will be much appreciated.

Respectfully,

F. M. HARLESS,

Internal Revenue Agent in Charge.

Enclosures:

Report of examination.

Form of acknowledgment. [37]

Examining Officer: L. D. Flint

Office Audit
San Francisco, California
May 1, 1941

Name and Address on return:

Lorin A. Cranson
215 Market Street
San Francisco, California

Returned filed: March 13, 1937 Year: 1936

District filed: First California Claim disallowed

Net income disclosed by RAR dated 9-21-39		14,883.50
No change in income.		
An amended claim was filed on the basis that dividends from Honolulu Oil Corp. were partially nontaxable and that a loss of $1,000.00 was sustained on stock of the Santa Clara Holding Co.		
Information on file shows that dividends from Honolulu Oil received in 1936 are 100% taxable.		
In report dated 9-21-39, Revenue Agent Oram allowed the loss of $1,000.00 on the stock. It is recommended that the amended claim be disallowed.		
Net income as adjusted		14,883.50
Less: Personal exemption	1,000.00	
Credit for dependents	400.00	1,400.00
Balance, surtax net income		13,483.50
Less: Earned income credit (10% of $14,000.00)		1,400.00
Balance, subject to normal tax		12,083.50
Normal tax at 4% on $12,083.50	483.34	
Surtax on $13,483.50	558.68	
Total tax		1,042.02
Tax liability as adjusted		1,042.02
Tax previously assessed	1,017.38	
Subsequent: List 1938-March 510348	149.48	1,166.86
Overassessment allowed 2-26-40	124.84	1,042.02
Overassessment		None

L. D. FLINT
Internal Revenue Auditor [38]

Treasury Department
Washington
Office of
Commissioner of Internal Revenue

Address Reply To
Commissioner of Internal Revenue
And Refer To
IT:C1:CC:4-CCP Jul 22 1941

Mr. L. A. Cranson,
215 Market Street,
San Francisco, California.

In re: Claim for refund of $176.68
For the year 1936

Sir:

Reference is made to the revenue agent's report upon an investigation of your tax liability dated May 1, 1941, a copy of which was forwarded you, wherein you were informed that the claim for refund indicated above will be disallowed.

In accordance with the provisions of existing internal revenue law, notice is hereby given of the disallowance of your claim in full.

Respectfully,
GUY T. HELVERING,
Commissioner,
By T. MOONEY
Deputy Commissioner. [39]

EXHIBIT F

[Printer's Note: Exhibit "F" is not set out here, as it is identical with Exhibit "C", the Second Amended Claim, attached to the Complaint, and printed in full at page 20 of this printed record.]

EXHIBIT G

Treasury Department
Office of
Commissioner of Internal Revenue

Address Reply To
Commissioner of Internal Revenue
And Refer To
IT:C1:CC:3-EVL Feb 10 1942

Mr. L. A. Cranson,
215 Market Street,
San Francisco, California.

Sir:

Reference is made to Form 843 filed by you on May 17, 1941, with the Collector of Internal Revenue, San Francisco, California, requesting a refund of $176.68, income tax, for the year 1936. The Form 843 is considered an application for reconsideration of your claim for refund, which was disallowed, registered notice of disallowance having been mailed on July 22, 1941, in accordance with the provisions of the Internal Revenue Laws.

The Bureau has considered the additional arguments presented in your Form 843, and in accordance with the findings of the Internal Revenue

Agent in Charge, San Francisco, California, the disallowance of the above-mentioned claim is sustained.

In view of the foregoing, your application for reconsideration is denied.

Respectfully,

TIMOTHY C. MOONEY,
Deputy Commissioner,
By T. C. ATKESON
Head of Division. [42]

EXHIBIT H

HONOLULU OIL CORPORATION

ASSETS ACQUIRED AND LIABILITIES ASSUMED UPON LIQUIDATION OF CERTAIN WHOLLY OWNED "SUBSIDIARIES" IN 1936

ASSETS AT COST	California Exploration Company, Inc.	Sea Cliff Development Company, Ltd.	Processco, imited	Total
Cash	$ 2,015.70	$	$	$ 2,015.70
Accounts Receivable—Less Reserve	50.96			50.96
Inventories:				
Crude Oil	1,780.86	1,573.04		3,353.90
Materials & Supplies	12,668.45			12,668.45
Oil Leases and Royalties—Less Reserve	112,262.94	38,278.32		150,541.26
Equipment—Less Reserve	62,926.38	151,818.49		214,744.87
Patents—Less Reserve			82,906.15	82,906.15
Incomplete Wells		245.50		245.50
	$191,705.29	$191,915.35	$ 82,906.15	$466,526.79
LIABILITIES				
Accrued Liabilities	1,701.47	110.69		1,812.16
Net Assets Acquired	$190,003.82	$191,804.66	$ 82,906.15	$464,714.63

[Endorsed]: Filed Feb. 11, 1943. [43]

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above-entitled cause having come regularly on for trial before the Court, sitting without a jury, the plaintiff appearing by his Attorneys, Leon de Fremery, Esq. and Messrs. Morrison, Hohfeld, Foerster, Shuman & Clark, the defendant appearing by Frank J. Hennessy, United States Attorney for the Northern District of California, represented by Esther B. Phillips, Assistant United States Attorney, and the facts having been stipulated and the cause having been argued and submitted, the Court now makes these

FINDINGS OF FACT

The Court refers to and incorporates herein as his findings the Stipulation of Facts made and filed by the parties. [44]

From the facts so stipulated and found, the Court renders the following

CONCLUSIONS OF LAW

(1) That the operating deficits of the wholly owned subsidiary corporations of Honolulu Oil Corporation as of the date of their liquidation did not diminish the earnings or profits of Honolulu Oil Corporation which were otherwise available for distribution to the stockholders of Honolulu Oil Corporation during the tax year.

(2) The loss sustained by Honolulu Oil Corporation upon the liquidation of its wholly owned subsidiary corporations did not diminish the earnings or profits of Honolulu Oil Corporation available for dividends during the tax year.

(3) The retroactive application of the Internal Revenue Code as amended by Section 501 of the Second Revenue Act of 1940 is not unconstitutional.

(4) The Commissioner of Internal Revenue correctly determined that the claim for tax refund should be rejected.

Let judgment be entered accordingly, without costs to either party.

MICHAEL J. ROCHE,
United States District Judge.

(Receipt of Service.)

[Endorsed]: Filed Oct. 23, 1943. [45]

In the District Court of the United States for the Northern District of California, Southern Division

No. 22168-R

LORIN A. CRANSON,

Plaintiff,

vs.

THE UNITED STATES OF AMERICA,

Defendant.

JUDGMENT

The above entitled cause having come regularly on for trial before the court, sitting without a jury, the plaintiff appearing by his attorneys, Leon de Fremery, Esq., and Messrs. Morrison, Hohfeld, Foerster, Shuman & Clark, the defendant appearing by Frank J. Hennessy, United States Attorney for the Northern District of California, represented by Esther B. Phillips, Assistant United States Attorney, and the facts having been stipulated and the cause having been argued and submitted, the Court having ordered judgment for defendant, It Is Hereby Ordered that judgment be entered for defendant without costs.

MICHAEL J. ROCHE,
United States District Judge.

[Endorsed]: Filed Oct. 25, 1943. [46]

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice Is Hereby Given that Lorin A. Cranson, plaintiff above named, hereby appeals to the United States Circuit Court of Appeals for the Ninth Circuit from the final judgment entered in this action on October 23, 1943.

Dated: November 18, 1943.

LEON de FREMERY
MORRISON, HOHFELD,
FOERSTER, SHUMAN
& CLARK
Attorneys for Appellant,
LORIN A. CRANSON
Address: Eleventh Floor,
Crocker Building
San Francisco, California

[Endorsed]: Filed Nov. 18, 1943 [47]

[Title of District Court and Cause.]

DESIGNATION OF RECORD

Appellant designates the following portions of the record, proceedings and evidence to be contained in the record on appeal in this action:

1. Complaint.
2. Defendant's Answer to Complaint.
3. Stipulation of Facts.

4. Findings of Fact and Conclusions of Law filed October 23, 1943. [48]
5. Judgment.
6. Notice of Appeal.
7. This Designation.

Dated: November 18, 1943.

LEON de FREMERY
MORRISON, HOHFELD,
FOERSTER, SHUMAN
& CLARK
Attorneys for Appellant,
LORIN A. CRANSON
Address: Eleventh Floor,
Crocker Building
San Francisco, California

Receipt of a copy of the within Designation of Record is hereby admitted this 18th day of November, 1943.

FRANK J. HENNESSY
Per T.S.
Attorney for Appellee

[Endorsed]: Filed Nov. 18, 1943. [49]

District Court of the United States
Northern District of California

CERTIFICATE OF CLERK TO TRANSCRIPT OF RECORD ON APPEAL

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of

California, do hereby certify that the foregoing 49 pages, numbered from 1 to 49, inclusive, contain a full, true, and correct transcript of the records and proceedings in the case of Lorin A. Cranson, Plaintiff, vs. United States of America, Defendant. No. 22168-S, as the same now remains on file and of record in my office.

I further certify that the cost of preparing and certifying the foregoing transcript of record on appeal is the sum of Six-dollars and thirty-five-cents ($6.35) and that the said amount has been paid to me by the Attorney for the appellant herein.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 22nd day of December A. D. 1943.

[Seal] C. W. CALBREATH
Clerk
WM. J. CROSBY
Deputy Clerk

[Endorsed]: No. 10644. United States Circuit Court of Appeals for the Ninth Circuit. Lorin A. Cranson, Appellant vs. United States of America, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Northern District of California Southern Division.

Filed December 23, 1943.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals
For the Ninth Circuit

No. 10644

LORIN A. CRANSON,

Appellant,

vs.

THE UNITED STATES OF AMERICA,

Appellee.

STATEMENT OF POINTS AND DESIGNATION OF RECORD

Statement of Points Relied Upon by Appellant

This is an action for the refund of income taxes paid with respect to certain distributions received from Honolulu Oil Corporation, which distributions appellant contends were in part at least distribu-

tions of capital and not subject to income tax. Appellant hereby states that the points upon which he intends to rely on this appeal are as follows:

(1) The court below erred in concluding that the operating deficits of the wholly owned subsidiary corporations of Honolulu Oil Corporation as of the date of their liquidation did not diminish the earnings or profits of Honolulu Oil Corporation which were otherwise available for distribution to the stockholders of Honolulu Oil Corporation during the tax year.

(2) In the event that the court below did not err as stated in paragraph (1) above, then the court below erred in concluding

(a) that the loss sustained by Honolulu Oil Corporation upon the liquidation of its wholly owned subsidiary corporations did not diminish the earnings or profits of Honolulu Oil Corporation available for dividends during the tax year; and

(b) that the retroactive application of the Internal Revenue Code as amended by Section 501 of the Second Revenue Act of 1940 is not unconstitutional.

(3) The court below erred in concluding that the Commissioner of Internal Revenue correctly determined that the claim for tax refund should be rejected.

(4) The court below erred in failing and refusing to render judgment for plaintiff.

Designation of Record to be Printed

Appellant hereby designates the entire record on appeal, excepting only the exhibits attached to the Stipulation of Facts, as necessary for the consideration of the foregoing points and as the portion of the record to be printed.

Dated: December 23, 1943.

LEON de FREMERY
MORRISON, HOHFELD,
FOERSTER, SHUMAN
& CLARK
Attorneys for Appellant
Eleventh Floor,
Crocker Building
San Francisco, California

Receipt of a copy of the within Statement of Points and Designation of Record is hereby admitted this 23rd day of December, 1943.

FRANK J. HENNESSY
United States Attorney
Per T.S.
Attorney for Appellee

[Endorsed]: Filed Dec. 23, 1943. Paul P. O'Brien, Clerk.

No. 10,644

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

LORIN A. CRANSON,
Appellant,

vs.

THE UNITED STATES OF AMERICA,
Appellee.

APPELLANT'S OPENING BRIEF.

LEON DE FREMERY,
MORRISON, HOHFELD, FOERSTER,
SHUMAN & CLARK,
Crocker Building, San Francisco,
Attorneys for Appellant.

PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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(b) Under the doctrine of the Sansome case that the continuity of the corporate life as a continuing venture is not broken, no valid distinction can be drawn between operating deficits on the one hand and earnings or profits on the other hand..... 19

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(b) In the determination of earnings or profits available for dividends it is not material that the loss realized by Honolulu upon the liquidation of its subsidiaries occurred in a tax-free transaction and was not recognized for income tax purposes.. 34

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No. 10,644

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

LORIN A. CRANSON,
Appellant,

vs.

THE UNITED STATES OF AMERICA,
Appellee.

APPELLANT'S OPENING BRIEF.

STATEMENT OF JURISDICTION.

Appellant filed suit against the United States in the United States District Court for the Northern District of California, Southern Division, for the refund of income tax paid for the calendar year 1936 in the amount of $51.84. (R. 2-6.) The District Court had jurisdiction by virtue of the provisions of Section 24(20) of the Judicial Code (Title 28 U.S.C. Sec. 41(20), 36 Stat. 1093, 44 Stat. 121) which confers jurisdiction upon the District Courts concurrent with the Court of Claims, of all claims not exceeding $10,000, for the recovery of any Internal Revenue taxes alleged to have been erroneously or illegally assessed or collected or any sum alleged to have been excessive, or even if the claim exceeds $10,000 if the Collector of Internal Revenue by whom such tax was

collected is not in office as Collector of Internal Revenue at the time such suit is commenced.

The District Court rendered judgment in favor of the United States. (R. 60-61.) This Court has jurisdiction of this appeal to review the judgment of the District Court by virtue of the provisions of Section 128(a) of the Judicial Code. (Title 28 U.S.C. Sec. 225, 52 Stat. 779.)

STATEMENT OF THE CASE.

During the calendar year 1936 appellant received from Honolulu Oil Corporation dividends in the sum of $450. Appellant reported the full amount thereof on his income tax return for 1936 as taxable dividends received. (R. 28-29.) Appellant thereafter filed two claims for refund, each in the amount of $51.84, both claims being based on the ground that only $18 out of the $450 of said dividends received by appellant were taxable dividends, and that the balance of $432 was not paid out of the earnings or profits of said corporation and was not taxable to appellant. (R. 29-30.) Both of said claims for refund were disallowed by the Commissioner of Internal Revenue (R. 30-31), and appellant thereupon filed suit against the United States for the refund of said income taxes as hereinabove set forth.

The sole question involved in this appeal is the extent to which dividends declared by Honolulu Oil Corporation during the calendar year 1936 are subject to federal income tax. This is a test case brought on behalf of all stockholders of Honolulu Oil Corporation.

Two companion test cases have been filed for the purpose of determining the taxability of dividends declared by Honolulu Oil Corporation during the calendar years 1937 and 1938, respectively. These two cases are likewise on appeal to this Court and are entitled and numbered: J. F. Shuman v. The United States of America, No. 10,645, and Lorin A. Cranson v. The United States of America, No. 10,646. A stipulation has been filed in each of these two cases to abide by the decision of this Court in this case.

All three appeals involve the same question of law, which may be generally stated as follows: Where a corporation undertakes a new venture through the formation of a wholly owned subsidiary corporation, and the subsidiary is operated at a loss and is thereafter liquidated and dissolved, do the earnings of the parent corporation available for dividends remain undiminished by this unprofitable venture, with the result that distributions which are actually returns of capital are taxed to the stockholders as income? The District Court answered this question in the affirmative, and held that the unprofitable venture did not reduce the earnings of the parent corporation, which remained intact and unaffected by the loss sustained.

The facts giving rise to the foregoing question were stipulated, and found as stipulated by the Court below. The pertinent portion of the facts is as follows:

Honolulu Consolidated Oil Company was incorporated in 1910 under the laws of the State of California. In 1930 it was reincorporated under the laws of the State of Delaware as Honolulu Oil Corporation, Ltd. In 1937 the name of the corporation was changed to

Honolulu Oil Corporation. Both of said corporations will be referred to as "Honolulu". (R. 31.)

On August 31, 1936, Honolulu liquidated three wholly owned subsidiary corporations, hereinafter referred to as "Subsidiaries", and took over all their assets and assumed their liabilities. The liquidation of said wholly owned Subsidiaries was carried out under the nontaxable provisions of section 112(b)(6) of the Revenue Act of 1936. (R. 33.) One of said wholly owned Subsidiaries was California Exploration Company, Inc., which corporation resulted from the consolidation in 1934 of two prior wholly owned subsidiary corporations of Honolulu which had been formed by Honolulu to acquire and develop prospective oil properties in the States of Wyoming and Texas. (R. 31-32.) Another of said wholly owned Subsidiaries was Sea Cliff Development Company, Ltd., which had been formed by Honolulu to acquire and develop prospective oil properties in Ventura County, California. The third wholly owned subsidiary, Processco, Limited, was formed by Honolulu primarily to acquire and develop patents relating to the processing of crude petroleum. (R. 32.)

Each of said wholly owned Subsidiaries sustained operating losses during the period from their incorporation to their dissolution. In the case of California Exploration Company, Inc., both its predecessors also sustained operating losses up to the date of their consolidation in 1934, which operating deficits were carried forward on to the books of the consolidated company, California Exploration Company, Inc. The total operating deficits of said three wholly owned

Subsidiaries as of the date of their liquidation on August 31, 1936, was $1,205,451.61. (R. 36-37.)

Upon the liquidation of said wholly owned Subsidiaries and the transfer of all their assets to Honolulu, Honolulu realized a loss of $1,225,908.63.[1] (R. 33.)

In 1936, the year involved in this appeal, Honolulu paid cash distributions to its stockholders in the amount of $1.00 on each of its outstanding 937,743 shares of capital stock, or a total cash distribution of $937,743. (R. 38.) On January 1, 1936, Honolulu had available for dividends accumulated earnings or profits in the amount of $139,631.26. Honolulu's earnings or profits during the calendar year 1936 amounted to the sum of $931,553.82 before deducting any portion of said loss realized upon the liquidation of said Subsidiaries in the amount of $1,225,908.63, or before deducting the total operating deficits of said Subsidiaries in the amount of $1,205,451.61. (R. 38.)

It follows that if Honolulu's earnings or profits available for dividends are to be reduced by either said loss or said operating deficits it had no earnings during the calendar year 1936, and said distributions were in such case distributions of capital and not income to the recipients, except to the extent that effect

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[1]The difference between this loss of $1,225,908.63 and the total operating deficits of the subsidiaries in the amount of $1,205,-451.61, referred to in the previous paragraph, is due to a payment of $20,457.02 made by Honolulu to third parties for a contingent interest in the capital stock of Processco, Limited. (R. 34.)

must be given to the accumulated earnings as of January 1, 1936.[2]

QUESTION FOR DECISION.

Specifically stated, the question for decision in this appeal is whether the operating deficits of said wholly owned subsidiaries as of the date of their liquidation in 1936, in the aggregate amount of $1,205,451.61, were absorbed by Honolulu upon the nontaxable liquidation of said subsidiaries, thus resulting in a reduction of the earnings of Honolulu otherwise available for dividends; or, in the alternative, whether the loss realized by Honolulu upon the liquidation of said wholly owned subsidiaries in 1936, in the amount of $1,225,908.63, reduced the earnings of Honolulu available for dividends.

SPECIFICATION OF ERRORS.

In support of his appeal, appellant relies upon the following specification of errors:

(1) The Court below erred in concluding that the operating deficits of the wholly owned subsidiary corporations of Honolulu Oil Corporation as of the date of their liquidation did not diminish the earnings or

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[2]It would appear that the accumulated earnings as of January 1, 1936, in the amount of $139,631.26 should be reduced by the loss for the year 1936 prorated on a daily basis to March 14, 1936, the date of the payment of the first dividend, and that the remainder of said accumulated earnings would then be available for the payment of that dividend. The remaining three dividends in 1936 are entirely paid out of capital.

profits of Honolulu Oil Corporation which were otherwise available for distribution to the stockholders of Honolulu Oil Corporation during the tax year.

(2) In the event that the Court below did not err as stated in paragraph (1) above, then the Court below erred in concluding

(a) that the loss sustained by Honolulu Oil Corporation upon the liquidation of its wholly owned subsidiary corporations did not diminish the earnings or profits of Honolulu Oil Corporation available for dividends during the tax year; and

(b) that the retroactive application of the Internal Revenue Code as amended by Section 501 of the Second Revenue Act of 1940 is not unconstitutional.

(3) The Court below erred in concluding that the Commissioner of Internal Revenue correctly determined that the claim for tax refund should be rejected.

(4) The Court below erred in failing and refusing to render judgment for plaintiff.

SUMMARY OF ARGUMENT.

I. The operating deficits of said subsidiaries were absorbed by Honolulu upon the nontaxable liquidation of said subsidiaries.

(a) The principle established by *Commissioner v. Sansome* (60 Fed. (2d) 931 (C.C.A. 2), certiorari denied, 287 U. S. 667), *United States v.*

Kauffmann, 62 Fed. (2d) 1045 (C.C.A. 9), and succeeding cases is that nontaxable reorganizations do not break the continuity of the corporate life as a continuing venture, with the result that under the doctrine of these cases it is held that the earnings or profits of the transferor corporation are transferred intact to the successor or transferee corporation.

(b) Under the doctrine of the *Sansome* case, that the continuity of the corporate life as a continuing venture is not broken, no valid distinction can be drawn between operating deficits on the one hand and earnings or profits on the other hand.

II. If it is held that the operating deficits of said subsidiaries were not absorbed by Honolulu, then it is contended in the alternative that the loss realized by Honolulu upon the liquidation of said subsidiaries reduced the earnings of Honolulu available for dividends.

(a) The term "earnings or profits" is not synonymous with statutory net income.

(b) In the determination of earnings or profits available for dividends it is not material that the loss realized by Honolulu upon the liquidation of its subsidiaries occurred in a tax-free transaction and was not recognized for income tax purposes.

(c) The attempted retroactive application of section 501 of the Second Revenue Act of 1940 violates the due process clause of the Constitution.

ARGUMENT.

I.

THE OPERATING DEFICITS OF SAID SUBSIDIARIES WERE ABSORBED BY HONOLULU UPON THE NONTAXABLE LIQUIDATION OF SAID SUBSIDIARIES.

The question involved in this appeal is the extent to which the stockholders of Honolulu must report as subject to federal income tax certain distributions paid by Honolulu to its stockholders during the calendar year 1936. Thus the appeal involves the taxes payable by the *stockholders* of Honolulu rather than the taxes payable by *Honolulu*. This distinction is of vital importance because the stockholders' taxes depend upon the *earnings or profits* of Honolulu available for dividends, whereas the corporation's taxes depend upon the *statutory net income* of Honolulu. The earnings or profits of the corporation available for dividends are of course entirely distinct from its statutory net income. For example, tax-exempt income is not included in statutory net income subject to tax, but does of course increase earnings or profits available for dividends. On the other hand, nondeductible items such as federal income taxes and capital losses will not reduce statutory net income but will obviously reduce earnings or profits available for dividends. The distinction between earnings or profits and statutory net income is more fully discussed hereinafter under II (a).

The question involved, therefore, is the extent to which the stockholders of Honolulu are subject to tax upon the distributions received by them in 1936. The

gross income which is subject to the income tax, after the allowance of certain statutory deductions, is defined by section 22(a) of the Revenue Act of 1936 (Appendix, p. i) (the statute controlling the decision of this appeal) to include dividends, and the term dividends is defined by section 115(a) of the Act (Appendix, p. v) as a distribution out of the "earnings or profits" of a corporation, whether those of the taxable year or those accumulated since March 1, 1913. If a corporation declares dividends out of its earnings or profits, such dividends constitute income to the stockholders upon which they must pay taxes. On the other hand, if the corporation has no earnings or profits available for dividends, or if its dividends exceed the earnings or profits which are available, then to the extent that the dividends are not paid out of earnings or profits of the corporation such distributions do not constitute income to the stockholders and are received free from tax until such time as the tax-free distributions received exceed the cost of the stock to the stockholders.

(a) **The principle established by the Sansome case and succeeding cases is that nontaxable reorganizations do not break the continuity of the corporate life as a continuing venture, with the result that under the doctrine of these cases it is held that the earnings or profits of the transferor corporation are transferred intact to the successor or transferee corporation.**

Since the term "earnings or profits" is not defined by the statute, problems have arisen regarding the interpretation to be given this term. One of the earliest situations requiring judicial construction

was that arising in connection with the tax-free transfer of the assets and business of one corporation to another corporation. In 1921 a New Jersey corporation transferred all its assets to a new corporation, which assumed the liabilities of the old corporation and issued its shares to the shareholders of the old corporation. Prior to its reincorporation the old corporation had a large earned surplus available for dividends, and if this corporation had paid dividends the stockholders would obviously have paid taxes thereon. After the reincorporation the new corporation paid dividends to its stockholders, who were identically the same persons as the stockholders of the old corporation, and these stockholders contended that the dividends were tax-free, since the new corporation had no earnings of its own available for dividends. The question thus presented came up for decision in the Circuit Court of Appeals for the Second Circuit in *Commissioner v. Sansome,* 60 Fed. (2d) 931 (1932), certiorari denied, 287 U. S. 667. That Court, in an opinion by Judge Learned Hand, held that the new corporation had *acquired the earnings of the old corporation* and the dividends were therefore subject to tax. The Court stated that the reincorporation was a nontaxable corporate reorganization under the express provisions of the statute making such reorganizations nontaxable, and came to the conclusion that nontaxable reorganizations do not break the continuity of the corporate life, saying:

> "Hence we hold that a corporate reorganization which results in no 'gain or loss' under Section 202(c)(2) (42 Stat. 230) *does not toll the com-*

> *pany's life as a continued venture* under Section 201, and that *what were 'earnings or profits' of the original, or subsidiary, company remain, for purposes of distribution, 'earnings or profits' of the successor, or parent, in liquidation."* (Italics added.)

Commissioner v. Sansome is the leading case on the subject of the transfer of corporate earnings from one corporation to another corporation in a nontaxable reorganization, the principle established by that case being known as the Sansome Rule.

Shortly after the decision of the Second Circuit Court of Appeals in *Commissioner v. Sansome* the same question arose in this Circuit in *United States v. Kauffmann,* 62 Fed. (2d) 1045 (1933). In that case the Union Lithograph Company, of San Francisco, which had a capital of $100,000 and an earned surplus of $419,258.12, transferred all its assets and liabilities to a new corporation, which issued its stock to the stockholders of the old corporation. On its books the new corporation credited $400,000 to capital stock and $119,258.12, the balance of the total capital and earned surplus of the old corporation, to paid-in surplus. After this reorganization and before the new corporation acquired any earnings or profits from its business, the new corporation declared a dividend, Kauffmann receiving $19,620, which he claimed did not constitute taxable income. The District Court, in an opinion by Judge St. Sure, rendered judgment for Kauffmann on the theory that the $19,620 was a distribution of the capital of the new corporation and not a dividend derived from earnings or profits.

On appeal, this Court first pointed out that the transaction by which the new corporation succeeded to all the assets and liabilities of the old corporation was a nontaxable reorganization, and then stated that the question involved was whether the earnings of the old corporation lost their character as such, when transferred to the new corporation, and became capital of the new corporation, or retained their character as earnings, so that a distribution thereof by the new corporation would be taxable. Kauffmann relied on the argument that the new corporation was a legal entity separate and distinct from the old corporation, and that therefore the earned surplus of the old corporation when transferred to the new corporation became a part of the capital of the new corporation. In deciding against this contention the Court relied on *Commissioner v. Sansome,* supra, which it said had decided that in a reorganization of this character there

> "was not such a change in corporate identity as prevented the new company from being considered as a *continuing venture* * * * and that whatever were earnings of the original corporation continued to be such in the hands of the new corporation." (Italics added.)

The principle that nontaxable reorganizations do not break the continuity of the corporate life as a continuing venture applies to consolidations of two or more corporations. In *Baker v. Commissioner,* 80 Fed. (2d) 813 (C.C.A. 2, 1936), where a parent corporation consolidated five wholly owned subsidiaries into a new company, it was held that the earnings of the

five subsidiaries were transferred intact to the successor corporation.

Many cases could be cited in support of this principle, but no purpose would be served in multiplying citations since there are no cases to the contrary, and the Sansome Rule is now recognized as an established principle of income tax law. The principal cases are cited in par. 9.58 of Mertens' new twelve-volume work on the Law of Federal Income Taxation, published in the latter part of 1942. With respect to liquidations, Mertens states (Vol. I, pp. 507-8):

> "In a tax-free liquidation of a subsidiary into a parent corporation, the earnings or profits of the former are not considered distributed but simply transferred intact to the parent. The theory of continued identity of earnings obtains also where there is more than one transferor."

The tax-free liquidation of a subsidiary into a parent corporation was first permitted under the Revenue Act of 1936, which added subsection (6) to section 112(b) of the statute as it existed prior thereto.[3] The pertinent portion of this subsection reads as follows:

> "(6) **Property received by a corporation on complete liquidation of another.**—No gain or loss shall be recognized upon the receipt by a corporation of property distributed in complete liquidation of another corporation." (Set forth in full, Appendix, p. i.)

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[3]Section 110(a) of the Act of 1935 (49 Stat. 1020) made a similar amendment to the 1934 Act, but this amendment never was actually effective, since it was applicable only to taxable years beginning after December 31, 1935, and was superseded by the Revenue Act of 1936.

Section 112(b)(6) as thus enacted continued in the same form in the Revenue Act of 1938 and thereafter in the Internal Revenue Code.

After the Sansome Rule became recognized as an established principle of income tax law, the Treasury Regulations were amended to incorporate this principle. Regulations 94, issued under the Revenue Act of 1936, contains the following provision:

> "Art. 115-11. **Effect on earnings or profits on (of) certain tax-free exchanges and tax-free distributions.**—If, under the law applicable to the year in which any transfer or exchange of property after February 28, 1913, was made (including transfers in connection with a reorganization *or a complete liquidation under section 112(b)(6)* * * *), gain or loss was not recognized * * *, then proper adjustment and allocation of the earnings or profits of the transferor shall be made as between the transferor and transferee corporations." (Italics added.) (Set forth in full, Appendix, p. x.)

The foregoing regulation applies by its terms to transactions other than the complete liquidation of a subsidiary corporation, but with respect to the complete liquidation of a subsidiary corporation, which of course necessarily results in the dissolution of the subsidiary, it is obvious that the only "proper adjustment and allocation of the earnings or profits of the transferor" which can be made as between the transferor and transferee corporations is the transfer of all the earnings or profits of the subsidiary to the parent corporation. In this respect the regulation is

but a recognition of the general principle referred to above as having been established by the cases, namely, that nontaxable reorganizations do not break the continuity of the corporate life as a continuing venture.

The quoted portion of Article 115-11 of Regulations 94 was continued without change in Regulations 101 relating to the Revenue Act of 1938 and Regulations 103 relating to the Internal Revenue Code. However, the following addition to Article 115-11 was made in 1938 by Regulations 101, and appeared immediately following the portion quoted above:

> "The general rule provided in section 115(b) that every distribution is made out of earnings or profits to the extent thereof and from the most recently accumulated earnings or profits, does not apply to:
>
> (1) * * *
>
> (2) The distribution in any taxable year (beginning before January 1, 1938, or on or after such date) of stock or securities, or other property or money, to a corporation *in complete liquidation of another corporation,* under the circumstances described in section 112(b)(6) of the Revenue Act of 1936 or section 112(b)(6) of the Revenue Act of 1938.
>
> (3) * * *
>
> (4) * * *
>
> A distribution described in paragraph (1), *(2),* (3) or (4) above does not diminish the earnings or profits of any corporation. In such cases, *the earnings or profits remain intact and available for distribution as dividends* by the corporation making such distribution, or *by another corpora-*

tion to which the earnings or profits are transferred upon such reorganization or other exchange." (Italics added.) (Set forth in full, Appendix, p. x.)

The addition thus made to the regulations in 1938 is merely a clarification of the portion of the regulation heretofore quoted (supra, p. 15) as it existed in 1936 and as continued in 1938. The portion of the regulation heretofore quoted could only mean, as applied to the complete liquidation of a subsidiary corporation, that the earnings or profits of the subsidiary would be transferred to the parent corporation. The addition made in 1938, quoted above, is more specific, and, as applied to the facts of our case, after stating that the distribution in liquidation by the three subsidiary corporations of Honolulu does not diminish the earnings or profits of the subsidiaries, continues with the statement that the earnings or profits remain intact and available for distribution as dividends by the corporation to which the earnings or profits are transferred, namely, Honolulu.

The addition to the regulations thus made in 1938 was continued without change in Regulations 103 as issued under the Internal Revenue Code.

Thus ever since the Revenue Acts have permitted the tax-free liquidation of subsidiaries, beginning with the year 1936, the regulations have provided that the earnings or profits of the subsidiaries remain intact and are transferred to the parent corporation. At the same time the regulations also contained the following provision:

"Gains and losses within the purview of section 112 or corresponding provisions of prior Acts *are brought into the earnings and profits at the time and to the extent such gains and losses are recognized under that section.*" (Italics added.)

(See Article 115-3 of Regulations 94 and 101 and Section 19.115-3 of Regulations 103, Appendix, p. viii.)

Section 112 of the Revenue Act of 1936 referred to in this regulation permits "reorganizations" as therein defined (section 112(g), Appendix, p. iv) to be consummated without incurring income tax. This provision of the regulations is a companion provision to the provision referred to above (Article 115-11), and is part of the same general plan adopted by the regulations to synchronize the effect of tax-free reorganizations upon *earnings or profits,* available for dividends, as distinguished from taxable net income. As applied to the liquidation of subsidiaries, for example, if a subsidiary had an earned surplus and its liquidation resulted in a profit to the parent, it is obvious that the earned surplus of the parent should not be increased by *both* the earned surplus of the subsidiary and the profit which is actually *realized* by the parent, although not *recognized* for tax purposes. Thus the regulations provide that the earned surplus will be transferred, but on the other hand realized profit (not recognized under section 112 as subject to tax) will not be taken into account in the computation of earnings or profits available for dividends.

What is the result if the subsidiary has an operating deficit and its liquidation results in a loss to the parent corporation?

(b) Under the doctrine of the Sansome case, that the continuity of the corporate life as a continuing[4] venture is not broken, no valid distinction can be drawn between operating deficits on the one hand and earnings or profits on the other hand.

Before discussing the effect of an operating deficit in the transferor corporation, the meaning of the terms "earnings available for dividends" and "operating deficit" must be clearly understood. A corporation has earnings available for dividends if its profits, after deducting dividends declared out of profits, exceed its losses. In such case the balance of its earned surplus account will appear on the right-hand or credit side. Since the earned surplus account normally appears on the right-hand or liability side of the balance sheet, together with capital stock, paid-in surplus, and other "net worth" accounts, an earned surplus account with a balance on the right or credit side would be said to have a positive rather than a negative balance. On the other hand, a corporation has an operating deficit if its operating losses exceed its profits after deducting dividends declared out of the profits. In this case the balance in its earned surplus account will appear on the left-hand or debit side. Such a balance would be said to be a negative balance in the earned surplus account.

It will perhaps be helpful to illustrate the foregoing by the following simple examples:

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[4] Judge L. Hand in the *Sansome* case uses the word "continued", whereas Judge Wilbur in the *Kauffmann* case changed the word to "continuing".

Assume that the X Company had earnings available for dividends on January 1, 1936, in the amount of $200,000, that its profits for 1936 were $50,000, and that it declared two $10,000 dividends during the year. Its earned surplus account would then appear as follows:

X Company

Earned Surplus

1936			1936		
June 1	Dividend	10,000	Jan. 1	Balance	200,000
Dec. 1	Dividend	10,000	Dec. 31	Profits, 1936	50,000
Dec. 31	Balance	230,000			
		250,000			250,000
			1937		
			Jan. 1	Balance	230,000

On the other hand, assume that the Y Company had an operating deficit on January 1, 1936, in the amount of $100,000, and that its earnings for 1936 were $60,000. Its earned surplus account would then appear as follows:

Y Company

Earned Surplus

1936			1936		
Jan. 1	Balance	100,000	Dec. 31	Profits, 1936	60,000
			Dec. 31	Balance	40,000
		100,000			100,000
1937					
Jan. 1	Balance	40,000			

It will be seen that the balance of the earned surplus account of Y Company on January 1, 1936, appeared on the left-hand or debit side, indicating that it had no earned surplus but on the contrary an operating deficit in the amount of $100,000. It thus had a negative balance in its earned surplus account. It will also be seen that the profits for 1936 in the amount of $60,000 operated to reduce this negative balance or operating deficit to the amount of $40,000, the balance appearing on January 1, 1937. This negative balance cannot be disregarded or charged to some other account, but must be carried in the *earned surplus* account, in order that the books will clearly indicate at what point subsequent profits have eliminated this adverse balance, after which additional profits will constitute earnings available for dividends. An operating deficit must be eliminated by subsequent earnings before there can be accumulated earnings or profits available for dividends (except that dividends may be paid from the current earnings of the taxable year). All the cases recognize this principle as basic. See for example,

Commissioner v. W. S. Farish & Co., 104 Fed. (2d) 833 (C.C.A. 5, 1939).

Thus the earned surplus account of a corporation constitutes an historical record of a corporation's annual profits and losses and the dividends which have been declared at such times as there were earnings available for dividends. The negative balances which may exist in this account from time to time, at which time the account will have an operating deficit, are just as much a part of this historical record as the

positive balances indicating earnings available for dividends.

To complete the picture we will assume that the following two balance sheets represent the condition of the X Company and the Y Company on January 1, 1936:

X Company

Balance Sheet, January 1, 1936

Assets		Liabilities	
Cash	5,000	Earned Surplus	200,000
Real Estate & Plant	1,495,000	Capital stock	1,300,000
	1,500,000		1,500,000

Y Company

Balance Sheet, January 1, 1936

Assets		Liabilities	
Cash	5,000	Earned Surplus	100,000
Real Estate & Plant	1,195,000	Capital Stock	1,300,000
	1,200,000		1,200,000

It will be seen that the earned surplus of the X Company appears in the foregoing balance sheet as a positive or black figure, whereas the earned surplus of the Y Company appears as a negative or red figure. As has been heretofore stated, under the doctrine of the *Sansome* case as set forth in numerous judicial decisions and as incorporated in the Treasury regulations, it is certain that upon the liquidation of a subsidiary corporation its earnings or profits are transferred to the parent corporation. Can any distinction be drawn between earnings and profits

which, as we have seen, represent a positive balance in the earned surplus account, and an operating deficit, which is a negative balance in the earned surplus account?

In the present case the three wholly owned subsidiaries of Honolulu had total operating deficits in the amount of $1,205,451.61, and Honolulu realized a loss upon the liquidation of these subsidiaries in the amount of $1,225,908.63 (the slight difference in these figures is explained in the footnote on page 5). It is apparent that the earned surplus of Honolulu should not be reduced by both the loss which it realized upon the dissolution of these subsidiaries and the total operating deficits of the subsidiaries, since this would be a duplication of the same loss. It is also apparent that in order to avoid a substantial overstatement of the earned surplus of Honolulu it is necessary to reduce its earned surplus either by the loss realized or by the operating deficits of the subsidiaries.

Article 115-3 of the regulations (supra p. 18) specifically refers to losses as well as gains, and provides that the loss realized by Honolulu will not reduce the earnings and profits of Honolulu because it was not recognized for tax purposes under section 112.[5] On the other hand, the companion provision of the regulations, namely, Article 115-11 (supra, p. 16), refers only to the transfer of the earnings or

[5]Although the decided cases do not agree with this Article, it has received statutory recognition. See the discussion under II (b) and (c), infra.

profits and not to the transfer of an operating deficit. These two articles, being part of the same general plan to synchronize the effect of tax-free reorganizations upon earnings or profits, must be read together. In view of the fact that Article 115-3 refers to losses as well as gains, it is quite possible that Article 115-11 should be interpreted to include operating deficits within the meaning of the words "earnings or profits". As we have seen, an operating deficit is but a negative balance in the earned surplus account, and such an interpretation would not be unreasonable.

We are merely suggesting but not insisting upon such an interpretation, since it is possible that the Treasury Department did not intend to go beyond the decided cases in promulgating this regulation. When the regulations first incorporated a provision relating to the transfer of earnings from one corporation to another in a nontaxable reorganization, which, as we have heretofore seen, occurred in 1936, the doctrine of the *Sansome* case had already become firmly established. The doctrine was recognized and discussed in Paul and Mertens' authoritative work on the Law of Federal Income Taxation (par. 8.45), which was published in 1934, but the doctrine of the *Sansome* case was not incorporated in Regulations 86, which appeared in 1935, and it was not until Regulations 94 were adopted in 1936 that this doctrine made its appearance in the provisions of Article 115-11 to which we have referred above. Thus the regulations merely followed the decided cases, which have dealt only with transferor corporations having earnings.

None of the cases thus far decided has dealt with an operating deficit, and it is possible, therefore, that the Treasury Department is waiting for decisions on this subject before expanding its regulations to definitely include operating deficits as well as earnings.

Since the principle upon which the transfer of earnings in a tax-free reorganization is based is that the *continuity of the corporate life as a continuing venture is not broken,* it is obvious that no logical distinction can be drawn between earnings and operating deficits. There is no magic in the figure being black rather than red. Suppose, for example, that X Company and Y Company, whose earned surplus accounts have been set forth above (p. 20), were to reorganize by means of a nontaxable statutory merger. If in such case Y Company was the continuing corporation and therefore did not cease to exist, its operating deficit in the amount of $100,000 would obviously not disappear but would continue on its books. On the other hand, the earnings of X Company in the amount of $200,000 would be transferred intact to Y Company in accordance with the Sansome Rule. Thus the earned surplus of the combined companies after the merger would show earnings available for dividends in the amount of $100,000, which would consist of the earnings of X Company less the operating deficit of Y Company.

If, on the other hand, X Company was the continuing corporation, then its surplus of $200,000 would of course continue on its books. But the parties to this proceeding differ as to the treatment to be

accorded the operating deficit of Y Company. It is our contention that, in accordance with the principle of the Sansome Rule that the continuity of the life of Y Company as a continuing venture is not broken, the operating deficit of Y Company would be transferred to X Company, thus reducing the earnings available for dividends of the combined corporations to $100,000, and producing the same result as though Y Company had been the continuing corporation. On the other hand, the Government, in attempting to make a distinction between operating deficits and earnings or profits, would contend that the operating deficit of Y Company would *not* be transferred to X Company in the merger, with the result that the combined corporations would have earnings of $200,000 available for dividends. Thus the Government is forced into the position of contending *that a different result obtains, depending upon whether X Company or Y Company is the continuing corporation.* The results of tax-free mergers should certainly not depend upon such insubstantial differences.

Taking an illustration more closely paralleling the facts of the instant case, let us suppose one of the wholly owned subsidiaries of Honolulu had had earnings of $1,000,000 and the remaining two subsidiaries had total operating deficits of $2,205,451.61, making a net operating deficit for the three subsidiaries of $1,205,451.61, which is the actual total operating deficit of the three wholly owned subsidiaries that were liquidated. In such case Honolulu would have sustained the same loss on the liquidation of the three subsidi-

aries as it actually sustained upon the liquidation of its three wholly owned subsidiaries in 1936, and this loss would have been substantially the same as the net operating deficits of the three subsidiaries in the total amount of $1,205,451.61. However, the Government, in accordance with the distinction that it attempts to make, would transfer the earned surplus of one of the subsidiaries, in the total amount of $1,000,000, but would refuse to permit the transfer of the operating deficits of the two other subsidiaries, in the amount of $2,205,451.61. Thus the earnings of Honolulu available for dividends would be *increased* by the amount of $1,000,000, whereas they should actually be *decreased* by the amount of $1,205,451.61. Not only is this result completely erroneous, but it is entirely illogical as well.

The illogical results to which the Government is forced in the two foregoing illustrations could be avoided by simply recognizing that earnings and operating deficits are both balances of the same account —one positive, the other negative. The illogical results flow from the Government's insistence on splitting the account down the middle and insisting that balances on one side of the middle are to be treated differently from balances on the other side.

To say that the earnings of the transferor corporation in a nontaxable reorganization are transferred intact to the successor corporation, but that this principle does not apply to operating deficits, is to confuse the *result* of the Sansome Rule, as such result has thus far appeared in the decided cases, which have

dealt only with corporations having an earned surplus, with the basic principle decided by the *Sansome* case, which principle has been reiterated in substantially all the later decisions which have passed upon this question. This basic principle is that in a tax-free reorganization *the continuity of the corporate life as a continuing venture is not broken.* This means that the entire taxable status of the corporation remains the same, that is to say, the basis of its assets, its reserves for depreciation and depletion, the status of its earned surplus account, whether a positive balance, indicating earnings available for distribution, or a negative balance, indicating an operating deficit, all these items and others of a similar character would be carried forward unchanged, some by specific statutory provisions, others by judicial construction through the application of the Sansome Rule. Thus the transfer of earnings in a corporate reorganization *is but one result of this basic principle,* and it is at once apparent that it is entirely illogical to assert, as the Government does, that the operating deficit of a corporation is in a different category from its earnings and will not be transferred to a successor corporation in accordance with the doctrine of the *Sansome* case.

Mertens in his new work on the Law of Federal Income Taxation states (Vol. I, p. 510):

> "Although there are no cases in point, the conclusions expressed above (relating to the transfer of earnings) would seem, if correct, to apply to the absorption of deficits of predecessor corporations as well as of surplus."

In conclusion, on this phase of the argument, it is recognized that the application of the Sansome Rule to *all* cases of tax-free reorganizations may also lead to illogical results—but if so, the results will be equally illogical whether operating deficits or earnings are involved. In other words, the illogical nature of these results will not be caused by treating operating deficits in the same manner as earnings, but rather may result from the application of the Sansome Rule to all cases of tax-free reorganizations. Mertens in the work just cited recognizes this possibility, and suggests that the test as to whether earnings are transferred to the successor corporation should not be the "tax-free" character of the so-called reorganization, stating that (Vol. I, p. 510):

> "any such general test would confuse the issue and give rise occasionally to absurd results in the various types of situations arising under our complex exchange and reorganization provisions. The proper test is whether there is substantial identity of the several corporations and continuity of proprietary interests."

This theory of Mertens is commented upon merely for the purpose of pointing out that even under this narrower application of the Sansome Rule, not adopted in any of the decided cases, the principle of the *Sansome* case would apply to the facts of the instant case. The three subsidiaries of Honolulu which were liquidated in 1936 were at all times wholly owned subsidiaries of Honolulu, and thus there was clearly "substantial identity of the several corporations and continuity of proprietary interests".

The argument that the operating deficits of these subsidiaries were absorbed by Honolulu applies, of course, with equal force to the acquisition by one of these subsidiaries, California Exploration Company, Inc., of the operating deficits of its two predecessors, also at all times wholly owned subsidiaries of Honolulu, which were carried forward on to the books of California Exploration Company, Inc. in the nontaxable consolidation which occurred in 1934. (See Statement of the Case, supra, p. 4.)

Our brief up to this point has been devoted exclusively to the argument that the operating deficits of the subsidiaries were absorbed by Honolulu. If we have established this point, and we believe that we have conclusively done so, it follows that Honolulu had no earnings during the calendar year 1936, and its distributions in that year were distributions of capital except to the extent set forth in footnote 2, supra, p. 6.

It is only in the event that the Court should conclude that the operating deficits of the subsidiaries were not absorbed by Honolulu that the alternative contention which we are about to discuss requires consideration.

II.

IF IT IS HELD THAT THE OPERATING DEFICITS OF SAID SUBSIDIARIES WERE NOT ABSORBED BY HONOLULU, THEN IT IS CONTENDED IN THE ALTERNATIVE THAT THE LOSS REALIZED BY HONOLULU UPON THE LIQUIDATION OF SAID SUBSIDIARIES REDUCED THE EARNINGS OF HONOLULU AVAILABLE FOR DIVIDENDS.

Honolulu sustained an admitted loss of $1,225,908.63 on the liquidation of its three wholly owned subsidiary corporations on August 31, 1936. The liquidation of these subsidiary corporations was carried out under the provisions of section 112(b)(6) of the Revenue Act of 1936 and was therefore nontaxable—that is to say, that neither gain nor loss was recognized in the determination of the *statutory net income* of Honolulu subject to income tax, as distinguished from its earnings or profits available for dividends.

(a) The term "earnings or profits" is not synonymous with statutory net income.

The fact that the liquidations were nontaxable transactions—that is, that Honolulu realized neither gain nor loss in so far as its *taxable net income* is concerned—does not necessarily mean that the loss realized thereon does not reduce the earnings of Honolulu available for dividends. The income tax statutes contain no definition of the words "earnings or profits" which are the source from which taxable dividends must be declared. That these words are not synonymous with the net income subject to taxation has been universally recognized ever since the

passage of the first income tax statute. Thus, for example, dividends received by one corporation on the stock which it owns in another corporation were for years entirely exempt from tax and therefore not included in the net income reported by the corporation receiving the dividends. Nevertheless, such dividends obviously increase earnings available for dividends of the recipient corporation. The same is true of any form of tax-exempt income. Many corporate expenses are also disallowed for income tax purposes, such as expenses which are not ordinary or necessary, salaries in an unreasonable amount, contributions in excess of a certain percentage of the net income, and federal income taxes. However, in all such cases it has always been recognized that the amount of the deductions which are not allowable in the calculation of net income subject to tax nevertheless do reduce earnings available for dividends.

A more apt illustration is perhaps the treatment accorded losses from sales of capital assets. Corporations have in the past been permitted a deduction for such losses only to the extent of $2000, and at the present time a deduction for losses from the sale of capital assets is not permitted at all, but such losses may only be used by corporations as an offset against similar gains. But there has never been any question that such losses reduce the earnings of a corporation available for dividends.

The distinction between taxable net income and earnings or profits was clearly stated in an early decision of the Board of Tax Appeals, *Charles F.*

Ayer, 12 B.T.A. 284, 287 (1928). An often quoted extract from that opinion reads as follows:

> "Dividends and (on) stock of domestic corporations, interest on bonds and obligations of States and municipalities, and statutory exemptions are not a part of the statutory net income of a corporation, but are nevertheless a part of its earnings or profits and may form a part of ordinary dividends which are taxable when received by the stockholders. On the other hand, corporations frequently make expenditures which are not deductible from gross income for income-tax purposes, but which nevertheless reduce earnings or profits. It therefore follows that the earnings or profits mentioned in section 201 (a) of the Revenue Act of 1921 are not the equivalent of the taxable net income of the corporation."

Thus the mere fact that the loss sustained by Honolulu upon the liquidation of its wholly owned subsidiaries in 1936 was not deductible for income tax purposes does not mean that it was not deductible in the computation of the earnings of Honolulu available for dividends; in fact, in the absence of some specific statutory provision (and such provision was not enacted until 1940[6]) it would seem that all losses sustained by a corporation necessarily reduce its earnings which are available for dividends. As the Third Circuit Court of Appeals stated in *Commissioner v. F. J. Young Corporation,* 103 Fed. (2d) 137, 139 (1939):

> "Section 115(a) is simply a definition of the word 'dividend' and merely distinguishes be-

[6]See discussion under subhead (c), infra.

tween a distribution out of 'earnings and profits' and a distribution out of capital. *The words 'earnings or profits',* as therein used, *are words in common use, and 'are to be given their natural, plain, ordinary, and commonly understood meaning'.''* (Italics added.)

(b) In the determination of earnings or profits available for dividends it is not material that the loss realized by Honolulu upon the liquidation of its subsidiaries occurred in a tax-free transaction and was not recognized for income tax purposes.

The Board of Tax Appeals and the Courts have decided in a series of cases, there being no decisions to the contrary, that gains or losses realized in tax-free transactions which do not affect statutory net income, nevertheless increase or decrease earnings or profits available for dividends. The leading case on this subject is *Commissioner v. F. J. Young Corporation,* 103 Fed. (2d) 137 (C.C.A. 3, 1939), affirming 35 B.T.A. 860 (1937).

In that case Corporation A exchanged certain property which had a cost basis of $36,000 for stock of another corporation which had a market value of $957,000, thus realizing a profit of $921,000. This exchange was a nontaxable transaction carried out under the provisions of section 112(b)(5) of the Revenue Act of 1928 (45 Stat. 816), and thus the realized gain was not recognized for income tax purposes. Thereafter Corporation A declared a substantial dividend to its stockholders, of whom the Young Corporation was one. The earnings of Corporation A, apart from the unrecognized gain of $921,000 referred to above,

were not sufficient to cover this distribution, and the Government therefore contended that the distribution was a dividend only to the extent of such earnings, the balance being applied in reduction of the basis of Corporation A's stock owned by the Young Corporation and taxable to the extent that the gain exceeded such basis. Since intercorporate dividends were at that time fully exempt from tax, the Young Corporation contended that the profit of $921,000, although not recognized for income tax purposes, *nevertheless increased the earnings or profits of Corporation A,* and consequently such earnings or profits were sufficient to cover the distribution.

Both the Board of Tax Appeals and the Circuit Court of Appeals held that the profit of $921,000 realized by Corporation A increased its earnings or profits available for dividends, and that it was immaterial that this profit occurred in a nontaxable transaction and was not recognized for income tax purposes. The Circuit Court of Appeals in its opinion said:

> "The infirmity in the commissioner's reasoning lies in the falsity of his major premise, namely, that a gain which is not 'recognized' under section 112 (b) (5) may not be considered as 'earnings or profits' under section 115 (a).
>
> It cannot be doubted that a corporation which has acquired certain property for $36,000, and later trades or exchanges it for other property worth $957,000, *has made a profit within the ordinary sense of the term,* for a profit is generally understood as 'the excess of what is obtained over the cost of obtaining it'. 50 C. J. 644; Hentz v.

> Pennsylvania Company for Insurance on Lives, etc., 134 Pa. 343, 19 A. 685. Therefore, as a result of the exchange of securities mentioned above, Yeager realized a definite 'gain' or 'profit' and the fact that the revenue act failed to 'recognize' that as a taxable 'gain' could not alter the situation. (Italics added.)
>
> The very wording of section 112 (b) indicates that Congress was aware of the distinction between net income and *taxable* net income for the provision that certain 'gains' or 'profits' should not be 'recognized' in computing taxable income, shows that Congress realized that as commonly understood they were nevertheless 'gains' and 'profits'."

Other cases to the same effect are:

Commissioner v. McKinney, 87 Fed. (2d) 811 (C.C.A. 10, 1937), affirming 32 B.T.A. 450 (1935);

Susan T. Freshman, 33 B.T.A. 394, 401 (1935) (appeals dismissed C.C.A. 2, November 17, 1936, and C.C.A. 3, November 27, 1936);

Robert McCormick, Executor, 33 B.T.A. 1046, 1060 (February, 1936);

Commissioner v. W. S. Farish & Co., 104 Fed. (2d) 833 (C.C.A. 5, 1939), affirming 38 B.T.A. 150 (1938);

Dorothy W. Elmhirst, 41 B.T.A. 348 (1940).

It is admitted that Honolulu realized a loss of $1,225,908.63 upon the liquidation of the three subsidiary corporations in 1936. (Statement of the Case, supra, p. 5.) Although this transaction was carried out under the provisions of section 112(b)(6) of the

1936 Act and therefore the loss was not recognized for income tax purposes, it is clear, in view of the foregoing authorities, that this loss nevertheless reduced earnings or profits available for dividends. But the Government contends that in spite of the foregoing decisions, and there has not been a case to the contrary, the loss realized by Honolulu *does not* reduce its earnings or profits, because Congress more than four years later amended the statute so as to overcome the effect of the foregoing decisions. It remains, therefore, to consider the effect of the amendment made by the Second Revenue Act of 1940.

(c) The attempted retroactive application of section 501 of the Second Revenue Act of 1940 violates the due process clause of the Constitution.

As has just been stated, such cases as had passed upon the question were unanimously to the effect that gains and losses realized by corporations in nontaxable transactions, and which were not recognized for income tax purposes, nevertheless increased or decreased earnings or profits available for dividends. These decisions were contrary to a sentence appearing in Article 115-3 of the regulations to which we have previously referred (supra, p. 18), which provided that gains or losses are brought into the earnings and profits at the time and to the extent such gains and losses are recognized for income tax purposes. Section 501 of the Second Revenue Act of 1940 (Appendix, p. v) converts this regulation into a statutory provision. This section of the statute added subsection (l) to section 115 of the Internal Revenue Code, the pertinent portion reading as follows:

> "Gain or loss realized from the sale or other disposition (after February 28, 1913) of property by a corporation * * * shall increase or decrease the earnings and profits to, but not beyond, the extent to which such a realized gain or loss was recognized in computing net income under the law applicable to the year in which such sale or disposition was made."

The foregoing amendment to the Internal Revenue Code was made applicable by section 501(b) to taxable years beginning after December 31, 1938, which is the effective period of the Internal Revenue Code. However, subsection (c) of section 501 purports to make the amendment effective as though it were a part of each of the Revenue Acts *for all taxable years* prior to the Internal Revenue Code.

In discussing the foregoing amendment the Report of the Senate Finance Committee (76th Congress, 3rd Session, Report No. 2114, p. 25) states:

> "The requirement of section 501 that there shall be no increase or decrease in earnings and profits by reason of a wholly unrecognized gain or loss *is but another aspect of the principle under which the earnings and profits of the transferor become by reason of the transfer the earnings and profits of the transferee.*" (Italics added.)

The principle referred to in the foregoing quotation is of course the doctrine of the *Sansome* case, and it is thus apparent that Congress had decided to incorporate into the statute the provision of the regulations (Article 115-3) which the Board and the

Courts had refused to follow, in order to consummate the general plan of the regulations (heretofore referred to supra, p. 18) to synchronize the effect of tax-free reorganizations upon earnings or profits available for dividends. No doubt Congress expected this plan, which would synchronize the treatment of unrecognized gains or losses on the one hand, with the transfer of earnings in nontaxable reorganizations on the other hand, to produce an equitable result in all cases, otherwise it would hardly have provided that the amendment should operate retroactively *for all taxable years.* And perhaps it would produce an equitable result in all cases—at least it would in so far as the present cases are concerned—if the doctrine of the *Sansome* case applies, as we believe we have conclusively established, to operating deficits as well as to earnings. If operating deficits are not included within the doctrine of the *Sansome* case, it is difficult to perceive why this amendment included within its scope unrecognized *losses* as well as gains. For example, in the instant case this amendment prohibits the reduction of the earnings of Honolulu available for dividends by an *admitted loss actually realized* in the amount of approximately $1,225,000. The only possible justification for such a result is that an equivalent reduction in earnings is obtained by the application of the principle of the *Sansome* case to the operating deficits of the subsidiaries. But if it is held that the Sansome Rule is to be limited to the carrying forward of earnings, and does not apply to the carrying forward of an operating deficit, then the planned synchronization to which we have

referred fails and the statute is inequitable. In such case it is contended that the retroactive application of the amendment made by section 501(a) of the Second Revenue Act of 1940, as provided by section 501(c), to a transaction occurring more than four years prior thereto, is confiscatory and invalid and a violation of the due process clause of the Fifth Amendment of the Constitution of the United States.

It is recognized that retroactive income taxes have been sustained as constitutional where their retroactivity is limited to the taxable year in which the statute is passed, or even to the preceding year already closed. Thus in *United States v. Hudson,* 299 U.S. 498 (1937), the Supreme Court said:

> "As respects income tax statutes, it long has been the practice of Congress to make them retroactive for relatively short periods so as to include profits from transactions consummated while the statute was in process of enactment, or within so much of the calendar year as preceded the enactment; and repeated decisions of this Court have recognized this practice and sustained it as consistent with the due process of law clause of the Constitution."

And in *White Packing Company v. Robertson,* 89 Fed. (2d) 775 (C.C.A. 4, 1937), it was held that the Act of Congress approved June 22, 1936, imposing the so-called "windfall tax", was valid, although applying to income received during the taxable year 1935, so as to be retroactive for a maximum period of about sixteen months.

It is obvious, of course, that no question of constitutionality can arise with respect to retroactive

amendments that are of benefit to taxpayers, such as the allowance of non-business expenses incurred in the production of income, and the elimination from gross income of recoveries of bad debts which had previously been deducted in loss years. Both of these amendments were enacted by the Revenue Act of 1942 (sections 121 and 116, respectively) (56 Stat. 812, 819) and were made retroactive under all prior statutes.

But with respect to amendments which are a burden to the taxpayer, the cases uniformly set forth the principle, illustrated by the two cases cited, that income tax amendments may be made retroactive for a period that is "recent". As to what is "recent", it would appear from the cases that the entire calendar year preceding the year of enactment of the statute—that is to say, a maximum period of twenty-four months—would be held to be recent.

One case has been found which sets forth an exception to this principle. This is the case of *Wilgard Realty Company, Inc. v. Commissioner,* 127 Fed. (2d) 514 (C.C.A. 2, 1942). This case passed upon the constitutionality of section 213(f) of the Revenue Act of 1939 (53 Stat. 871), by which an amendment made by section 213 of that Act was made applicable to taxable years ending after December 31, 1923. The Supreme Court of the United States had held in *United States v. Hendler,* 303 U. S. 564 (1938), that the assumption of the liabilities of a corporate party to a tax-free reorganization destroys the nontaxable character of the reorganization, gain being recognized to the extent of the assumption. The amend-

ments made by section 213 of the 1939 Act were made to overcome the effect of the Supreme Court decision and to permit the assumption by one corporation of the debts of the other in the process of reorganization. The taxpayer in the *Wilgard* case had acquired certain real estate in 1932 from an individual in exchange for all the taxpayer's stock, together with the assumption of the individual's liability on a debt secured by a mortgage on the real estate. The taxpayer sold this real estate in 1937, and contended that in computing its gain or loss on this sale it was not limited to the cost of the real estate to the individual transferor, as it would be if the exchange which occurred in 1932 was tax-free. The exchange was tax-free if the amendments made by section 213 of the 1939 Act could be applied retroactively, but the taxpayer contended that the retroactive provisions of section 213(f) of the Act violated the Fifth Amendment of the Constitution.

In discussing the extent to which an income tax statute may be retroactive in its operation, the Court said (p. 517):

> "Sometimes the extent of permissible retroactivity can be measured with sufficient certainty in terms of time. As for instance, the 'recent transactions' as to which a retroactive tax law might be valid under Cooper v. United States, 280 U. S. 409, 411, 50 S. Ct. 164, 74 L. Ed. 516, were in Welch v. Henry, supra, at page 150 of 305 U. S., at page 127 of 59 S. Ct., 83 L. Ed. 87, 118 A. L. R. 1142, 'taken to include the receipt of income during the year of the legislative session preceding that of its enactment'. Taxpayers must

> expect that fundamental changes in tax laws may be made at any time in a taxable period to be effective for the entire period and in addition for some time previously, as the above cases show. That is to say, retroactivity in taxation which would otherwise be so arbitrary as to be unconstitutional may escape such disability if it is not too great in point of time."

However, the taxpayer in the *Wilgard* case undoubtedly believed when it acquired the real estate in 1932 that the transaction was tax-free, contrary to the contention which it was advancing, since no case prior to the decision of the Supreme Court in the *Hendler* case in 1938 had held that such a transaction was taxable because of the assumption of liabilities. The Court considers the effect of this situation in the following language (p. 517):

> "Sec. 213(f)(1) of the Revenue Act of 1939 was in terms made applicable to exchanges 'occurring in a taxable year ending after December 31, 1923, and beginning before January 1, 1939'. Its possible backward effect is, indeed, long and in this instance was about seven years. There is no reason, nevertheless, to believe that the petitioner made the exchange in 1932 in the belief that its assumption of the mortgage indebtedness kept the exchange from being a tax free one. On the contrary it is but a fair deduction from the undisputed facts that the petitioner believed the exchange was, when it occurred, the tax free one that the 1939 enactment made it."

The Court then sustained the retroactive effect of the amendment as constitutional, on the ground that

the taxpayer understood at the time the transaction was entered into that the effect would be no different *than that made by the retroactive amendment.* As the Court said (p. 517), "the decisive test in this instance is whether this taxpayer has had its expectations as to taxation unreasonably disappointed".

In the Report of the Ways and Means Committee of the House of Representatives (76th Congress, 1st Session, Report No. 855), the Committee on page 20 gives practically the same reason for making the amendment discussed in the *Wilgard* case retroactive as that referred to by the Court as justifying the retroactive application of the amendment. The Committee said, page 20:

> "Since transactions entered into under such Acts (Acts of 1924 to 1938, inclusive) were made under the understanding of the law that such assumptions of, and taking subject to, liabilities did not give rise to recognizable gain, *it is necessary, in order to prevent hardship on taxpayers and to prevent tax avoidance, to provide retroactively for the application of the rules above provided."* (Italics added.)

However, the situation with respect to the retroactive application of the amendment made by section 501 of the Second Revenue Act of 1940 is directly the reverse of that which existed in the amendment discussed in the *Wilgard* case. The appellant in the instant case had no reason to suppose that the loss realized by Honolulu in 1936 upon the liquidation of its subsidiaries would not reduce earnings or profits available for dividends. The decisions of the Board

of Tax Appeals as they existed at that time were uniformly to the effect that gains or losses incurred in tax-free transactions and not recognized for income tax purposes would nevertheless increase or decrease earnings or profits available for dividends. See the discussion under heading II (b), supra, and the cases therein cited.

In view of the foregoing authorities it would seem that section 501(b) of the Second Revenue Act of 1940, making the amendment to the Internal Revenue Code contained in section 501(a) retroactive for the effective period of the Code, that is to say, to January 1, 1939, covers a period which is "recent" and is therefore a proper exercise of the legislative power. With respect to section 501 (c), however, which purports to make the amendment operative *for all prior years,* if it should be held that the operating deficits of its subsidiaries were not transferred to Honolulu, then it is contended that a serious inequity results and that section 501 (c) is confiscatory in so far as this appellant is concerned, and in violation of the due process clause of the Constitution.

CONCLUSION.

The doctrine of the *Sansome* case is peculiarly applicable to the nontaxable liquidation of the three wholly owned subsidiaries of Honolulu because they meet the suggested narrower test of substantial identity of the several corporations and continuity of proprietary interests. Since under this doctrine the

continuity of the life of the subsidiaries is not broken, it irresistibly follows that the operating deficits of the subsidiaries were absorbed by Honolulu.

It is only in the event the Court does not concur in the foregoing contention, that the attempted retroactive application of section 501(a) of the Second Revenue Act of 1940 produces an inequitable result and is attacked as unconstitutional. All the cases agree in holding that the loss admittedly sustained by Honolulu reduces its earnings available for dividends. The attempt to overcome the effect of these decisions by a statute enacted more than four years after the loss was incurred is a violation of the due process clause of the Constitution.

Dated, San Francisco,
February 11, 1944.

Respectfully submitted,
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(Appendix Follows.)

Appendix.

Appendix

STATUTORY PROVISIONS.

Revenue Act of 1936, Section 22(a) (49 Stat. 1657).

(a) GENERAL DEFINITION.—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross income; and all Acts fixing the compensation of such Presidents and judges are hereby amended accordingly.

Revenue Act of 1936, Section 112(b)(6) (49 Stat. 1680).

(6) PROPERTY RECEIVED BY CORPORATION ON COMPLETE LIQUIDATION OF ANOTHER.—No gain or loss shall be recognized upon the receipt by a corporation of property distributed in complete liquidation of another corporation. For the purposes of this paragraph a distribution shall be considered to be in complete liquidation only if—

(A) the corporation receiving such property was, on the date of the adoption of the plan of liquidation, and has continued to be at all times until the receipt of the property, the owner of stock (in such other corporation) possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and the owner of at least 80 percentum of the total number of shares of all other classes of stock (except nonvoting stock which is limited and preferred as to dividends), and was at no time on or after the date of the adoption of the plan of liquidation and until the receipt of the property the owner of a greater percentage of any class of stock than the percentage of such class owned at the time of the receipt of the property; and

(B) no distribution under the liquidation was made before the first day of the first taxable year of the corporation beginning after December 31, 1935; and either

(C) the distribution is by such other corporation in complete cancellation or redemption of all its stock, and the transfer of all the property occurs within the taxable year; in such case the adoption by the stockholders of the resolution under which is authorized the distribution of all the assets of such corporation in complete cancellation or redemption of all its stock, shall be considered an adoption of a plan of liquidation, even though no time for the completion of the transfer of the property is specified in such resolution; or

(D) such distribution is one of a series of distributions by such other corporation in complete cancellation or redemption of all its stock

in accordance with a plan of liquidation under which the transfer of all the property under the liquidation is to be completed within three years from the close of the taxable year during which is made the first of the series of distributions under the plan, except that if such transfer is not completed within such period, or if the taxpayer does not continue qualified under subparagraph (A) until the completion of such transfer, no distribution under the plan shall be considered a distribution in complete liquidation.

If such transfer of all the property does not occur within the taxable year the Commissioner may require of the taxpayer such bond, or waiver of the statute of limitations on assessment and collection, or both, as he may deem necessary to insure, if the transfer of the property is not completed within such three-year period, or if the taxpayer does not continue qualified under subparagraph (A) until the completion of such transfer, the assessment and collection of all income, war-profits, and excess-profits taxes then imposed by law for such taxable year or subsequent taxable years, to the extent attributable to property so received. A distribution otherwise constituting a distribution in complete liquidation within the meaning of this paragraph shall not be considered as not constituting such a distribution merely because it does not constitute a distribution or liquidation within the meaning of the corporate law under which the distribution is made; and for the purposes of this paragraph a transfer of property of such other corporation to the taxpayer shall not be considered as not

constituting a distribution (or one of a series of distributions) in complete cancellation or redemption of all the stock of such other corporation, merely because the carrying out of the plan involves (i) the transfer under the plan to the taxpayer by such other corporation of property, not attributable to shares owned by the taxpayer, upon an exchange described in paragraph (4) of this subsection, and (ii) the complete cancellation or redemption under the plan, as a result of exchanges described in paragraph (3) of this subsection, of the shares not owned by the taxpayer.

Revenue Act of 1936, Section 112(g) (49 Stat. 1682).

(g) DEFINITION OF REORGANIZATION.—As used in this section and section 113—

(1) The term "reorganization" means (A) a statutory merger or consolidation, or (B) the acquisition by one corporation in exchange solely for all or a part of its voting stock: of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of another corporation; or of substantially all the properties of another corporation, or (C) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (D) a recapitalization, or (E) a mere change in identity, form, or place of organization, however effected.

(2) The term "a party to a reorganization" includes a corporation resulting from a reorganization and includes both corporations in the case

of a reorganization resulting from the acquisition by one corporation of stock or properties of another.

Revenue Act of 1936, Section 115(a) (49 Stat. 1682).

(a) DEFINITION OF DIVIDEND.—The term "dividend" when used in this title (except in section 203 (a) (3) and section 207 (c) (1), relating to insurance companies) means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.

Second Revenue Act of 1940 (54 Stat. 1004).

Sec. 501. EARNINGS AND PROFITS OF CORPORATIONS.

(a) UNDER INTERNAL REVENUE CODE.—Section 115 of the Internal Revenue Code is amended by inserting at the end thereof the following new subsections:

"(l) EFFECT ON EARNINGS AND PROFITS OF GAIN OR LOSS AND OF RECEIPT OF TAX-FREE DISTRIBUTIONS.—The gain or loss realized from the sale or other disposition (after February 28, 1913) of property by a corporation—

"(1) for the purpose of the computation of earnings and profits of the corporation, shall be determined, except as provided in paragraph (2), by using as the adjusted basis the adjusted basis (under the law applicable to the year in which

the sale or other disposition was made) for determining gain, except that no regard shall be had to the value of the property as of March 1, 1913; but

"(2) for the purpose of the computation of earnings and profits of the corporation for any period beginning after February 28, 1913, shall be determined by using as the adjusted basis the adjusted basis (under the law applicable to the year in which the sale or other disposition was made) for determining gain.

Gain or loss so realized shall increase or decrease the earnings and profits to, but not beyond, the extent to which such a realized gain or loss was recognized in computing net income under the law applicable to the year in which such sale or disposition was made. Where in determining the adjusted basis used in computing such realized gain or loss the adjustment to the basis differs from the adjustment proper for the purpose of determining earnings or profits, then the latter adjustment shall be used in determining the increase or decrease above provided. Where a corporation receives (after February 28, 1913) a distribution from a second corporation which (under the law applicable to the year in which the distribution was made) was not a taxable dividend to the shareholders of the second corporation, the amount of such distribution shall not increase the earnings and profits of the first corporation in the following cases:

"(1) No such increase shall be made in respect of the part of such distribution which (under such law) is directly applied in reduction of the basis

of the stock in respect of which the distribution was made.

"(2) No such increase shall be made if (under such law) the distribution causes the basis of the stock in respect of which the distribution was made to be allocated between such stock and the property received.

"(m) EARNINGS AND PROFITS—INCREASE IN VALUE ACCRUED BEFORE MARCH 1, 1913. (This subsection omitted as not material.)"

(b) EFFECTIVE DATE OF AMENDMENT.—The amendment made by subsection (a) shall be applicable to taxable years beginning after December 31, 1938.

(c) UNDER PRIOR ACTS.—For the purposes of the Revenue Act of 1938 or any prior Revenue Act the amendments made to the Internal Revenue Code by subsection (a) of this section shall be effective as if they were a part of each such Revenue Act on the date of its enactment. Nothing in this subsection shall affect the tax liability of any taxpayer for any year which, on September 20, 1940, was pending before, or was theretofore determined by, the Board of Tax Appeals, or any court of the United States.

REGULATIONS.

Regulations 94, Article 115-3.

Regulations 101, Article 115-3.

Regulations 103, Section 19.115-3.

Art. 115-3. **Earnings or profits.** In determining the amount of earnings or profits (whether of the taxable year, or accumulated since February 28, 1913, or accumulated prior to March 1, 1913) due consideration must be given to the facts, and mere bookkeeping entries increasing or decreasing surplus will not be conclusive. Among the items entering into the computation of corporate earnings or profits for a particular period are all income exempted by statute, income not taxable by the Federal Government under the Constitution, as well as all items includible in gross income under section 22(a) of the Act or corresponding provisions of prior acts.* Gains and losses within the purview of section 112 or corresponding provisions of prior Acts* are brought into the earnings and profits at the time and to the extent such gains and losses are recognized under that section. Interest on State bonds and certain other obligations, although not taxable when received by a corporation, is taxable to the same extent as other dividends when distributed to shareholders in the form of dividends.

In the case of a corporation in which depletion is a factor in the determination of income, the only depletion deductions to be considered in the computation of earnings or profits are those based on (1)

*Section 19.115-3 reads "prior Revenue Acts".

cost or other basis, if the depletable asset was acquired subsequent to February 28, 1913, or (2) adjusted cost or March 1, 1913, value, whichever is higher, if acquired prior to March 1, 1913. Thus, discovery and percentage depletion under all Revenue Acts for mines and oil and gas wells should not be taken into consideration in computing the earnings or profits of a corporation.

A loss sustained for a year prior to the taxable year does not affect the earnings or profits of the taxable year. However, in determining the earnings or profits accumulated since February 28, 1913, the excess of a loss sustained for a year subsequent to February 28, 1913, over the undistributed earnings or profits accumulated since February 28, 1913, and prior to the year for which the loss was sustained, reduces surplus as of March 1, 1913, to the extent of such excess. And, if the surplus as of March 1, 1913, was sufficient to absorb such excess, distributions to shareholders after the year of the loss are out of earnings or profits accumulated since the year of the loss to the extent of such earnings.

With respect to the effect on the earnings or profits accumulated since February 28, 1913, of distributions made on or after January 1, 1916, and prior to August 6, 1917, out of earnings or profits accumulated prior to March 1, 1913, which distributions were specifically declared to be out of earnings or profits accumulated prior to March 1, 1913, see section 31(b) of the Revenue Act of 1916, as amended by section 1211 of the Revenue Act of 1917.

Regulations 94, Article 115-11.

Art. 115-11. **Effect of earnings or profits on (of) certain tax-free exchanges and tax-free distributions.**— If, under the law applicable to the year in which any transfer or exchange of property after February 28, 1913, was made (including transfers in connection with a reorganization or a complete liquidation under section 112(b)(6) and intercompany transfers of property during a period of affiliation), gain or loss was not recognized (or was recognized only to the extent of the property received other than that permitted by such law to be received without the recognition of gain), then proper adjustment and allocation of the earnings or profits of the transferor shall be made as between the transferor and transferee corporations.

The general rule provided in section 115(b) that every distribution is made out of earnings or profits to the extent thereof and from the most recently accumulated earnings or profits, does not apply to:

(1) The distribution, in pursuance of a plan of reorganization, by or on behalf of a corporation a party to the reorganization, to its shareholders of stock or securities in such corporation or in another corporation a party to the reorganization—

(A) in any taxable year beginning before January 1, 1934, without the surrender by the distributees of stock or securities in such corporation (see section 112(g) of the Revenue Act of 1932); or

(B) in any taxable year (beginning before January 1, 1936, or on or after such date) in exchange for its stock or securities (see section 112(b)(3)

if no gain to the distributees from the receipt of such stock or securities was recognized by law.

(2) A stock dividend which was not subject to tax in the hands of the distributee because either it did not constitute income to him within the meaning of the sixteenth amendment to the Constitution or because exempt to him under section 115(f) of the Revenue Act of 1934 or a corresponding provision of a prior Revenue Act.

A distribution described in paragraphs (1) and (2) above does not diminish the earnings or profits of any corporation. In such cases, the earnings or profits remain intact and available for distribution as dividends by the corporation making such distribution, or by another corporation to which the earnings or profits are transferred upon such reorganization or other exchange.

For the purposes of this article, the terms "reorganization" and "party to the reorganization" shall, for any taxable year beginning before January 1, 1934, have the meanings assigned to such terms in section 112 of the Revenue Act of 1932, and for any taxable year beginning after December 31, 1933, and before January 1, 1936, have the meanings assigned to such terms in section 112 of the Revenue Act of 1934.

Regulations 101, Article 115-11.

Art. 115-11. **Effect on earnings or profits of certain tax-free exchanges and tax-free distributions.** If, under the law applicable to the year in which any transfer or exchange of property after February 28, 1913, was made (including transfers in connection with a reorganization or a complete liquidation under section 112(b)(6) and intercompany transfers of property during a period of affiliation), gain or loss was not recognized (or was recognized only to the extent of the property received other than that permitted by such law to be received without the recognition of gain), then proper adjustment and allocation of the earnings or profits of the transferor shall be made as between the transferor and transferee corporations.

The general rule provided in section 115(b) that every distribution is made out of earnings or profits to the extent thereof and from the most recently accumulated earnings or profits, does not apply to:

(1) The distribution, in pursuance of a plan of reorganization, by or on behalf of a corporation a party to the reorganization, to its shareholders of stock or securities in such corporation or in another corporation a party to the reorganization—

(A) in any taxable year beginning before January 1, 1934, without the surrender by the distributees of stock or securities in such corporation (see section 112(g) of the Revenue Act of 1932); or

(B) in any taxable year (beginning before January 1, 1938, or on or after such date) in

exchange for its stock or securities (see section 112(b)(3))

if no gain to the distributees from the receipt of such stock or securities was recognized by law.

(2) The distribution in any taxable year (beginning before January 1, 1938, or on or after such date) of stock or securities, or other property or money, to a corporation in complete liquidation of another corporation, under the circumstances described in section 112(b)(6) of the Revenue Act of 1936 or section 112(b)(6) of the Revenue Act of 1938.

(3) The distribution in any taxable year (beginning after December 31, 1937) of stock or securities, or other property or money, in the case of an exchange or distribution described in section 371 (relating to exchanges and distributions in obedience to orders of the Securities and Exchange Commission), if no gain to the distributees from the receipt of such stock, securities, or other property or money was recognized by law.

(4) A stock dividend which was not subject to tax in the hands of the distributee because either it did not constitute income to him within the meaning of the sixteenth amendment to the Constitution or because exempt to him under section 115(f) of the Revenue Act of 1934 or a corresponding provision of a prior Revenue Act.

A distribution described in paragraph (1), (2), (3), or (4) above does not diminish the earnings or profits of any corporation. In such cases, the earnings or profits remain intact and available for distribution as dividends by the corporation making such distribu-

tion, or by another corporation to which the earnings or profits are transferred upon such reorganization or other exchange. In the case, however, of amounts distributed in liquidation (other than a tax-free liquidation or reorganization described in paragraph (1), (2), or (3) above) the earnings or profits of the corporation making the distribution are diminished by the portion of such distribution properly chargeable to earnings or profits accumulated after February 28, 1913, after first deducting from the amount of such distribution the portion thereof allocable to capital account.

For the purposes of this article, the terms "reorganization" and "party to the reorganization" shall, for any taxable year beginning before January 1, 1934, have the meanings assigned to such terms in section 112 of the Revenue Act of 1932; for any taxable year beginning after December 31, 1933, and before January 1, 1936, have the meanings assigned to such terms in section 112 of the Revenue Act of 1934; and for any taxable year beginning after December 31, 1935, and before January 1, 1938, have the meanings assigned to such terms in section 112 of the Revenue Act of 1936.

No. 10,644

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United States Circuit Court of Appeals

For the Ninth Circuit

LORIN A. CRANSON,
Appellant,

vs.

THE UNITED STATES OF AMERICA,
Appellee.

APPELLANT'S PETITION FOR A REHEARING.

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PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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vs.

THE UNITED STATES OF AMERICA,
Appellee.

APPELLANT'S PETITION FOR A REHEARING.

To the Honorable Curtis D. Wilbur, Presiding Judge, and to the Honorable Associate Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

Appellant respectfully petitions this Court for a rehearing in this case on the following grounds:

1. The Court erred in stating in its written opinion rendered herein on January 24, 1945, that there has been no showing that any of the loss sustained by Honolulu Oil Corporation, Ltd., upon the liquidation of its subsidiaries, was incurred in the tax year in question, namely 1936. *It is stipulated* (R. 33) *that the subsidiaries were liquidated on August 31, 1936, and that upon said liquidation Honolulu realized a loss of $1,225,908.63,* the entire amount of the loss in question. (Appellant's Opening Brief, p. 5.) As a result of

said misconception of the facts, the Court has dismissed without consideration appellant's alternative contention that the loss realized by Honolulu upon the liquidation of the subsidiaries reduced the earnings of Honolulu available for dividends.

2. The Court erred in stating that it is admitted that $931,553.82 earnings or profits were made in 1936 by the parent corporation. *It is stipulated* (R. 38) *that these are the earnings before deducting the loss of $1,225,908.63 realized in 1936 upon the liquidation of the subsidiaries.* Thus the *stipulated fact* is that Honolulu had no earnings available for dividends in 1936, but sustained a loss in the amount of $294,354.81, completely eliminating the earnings of $139,631.26 as of January 1, 1936. (See footnote p. 2 Appellant's Reply Brief.) Thus the actual fact is that the dividends are distributions of capital *and not income to the recipients.* The Court below, having held that appellant must pay an income tax upon a return of capital, and having so held because of the provisions of section 501 of the Second Revenue Act of 1940, has necessarily decided that this statutory provision is constitutional in its application to this particular situation. Whether the lower Court's application of this statute violates the provisions of the Sixteenth Amendment of the Constitution of the United States in so far as appellant and the other stockholders of Honolulu are concerned is a matter necessarily involved in this case and therefore before this Court for decision. Appellant also contends that the attempted retroactive application of this statutory provision for a period of more

than four years is a violation of the due process clause of the Fifth Amendment of the Constitution of the United States. The Court has failed to pass upon this question.

3. The Court has misapplied the cases of *Long Beach Improvement Company,* 5 B.T.A. 590, and *Foley Securities Corporation,* 38 B.T.A. 1036. These cases are cited in support of the proposition that if Honolulu itself had had an operating deficit at the beginning of 1936, the deficit could not have been deducted *in ascertaining the earnings available in 1936 for the payment of dividends.* The *Foley Securities* case stands for exactly the reverse of this proposition, the Court there holding that a deficit as of December 31, 1933, in the amount of $23,650.53 *must be deducted* from 1934 earnings in the amount of $49,909.52 in order to determine the earnings available for dividends in 1934. The Court there held that only the remainder in the amount of $26,258.99 was available for dividends.[1] The *Long Beach* case holds that a corporation *is subject to tax* on its net income for the taxable year although such income is not sufficient to wipe out a preexisting deficit. It is apparent from the citation of this case that the Court is confusing the statutory net income upon which Honolulu must pay a tax, with the earnings of Honolulu available for dividends. That this confusion exists seems apparent from the statement in the Court's opinion reading: "The equation of operating deficit for tax

[1]The statutory definition of dividend was changed, however, in 1936 to read as set forth in the Court's opinion so that this case is no longer in point.

purposes is the loss sustained within the taxable year." If appellant is correct in interpreting this sentence to mean that for tax purposes the loss sustained within the taxable year constitutes the operating deficit for that year, then the Court has failed to appreciate that operating deficit (or operating profit) need bear no relationship whatsoever to the loss as computed for tax purposes (or taxable income). (Appellant's Opening Brief, pp. 31-37.) Furthermore, in that event the Court has failed to answer appellant's contention that the *total* accumulated operating deficits of the subsidiaries reduced Honolulu's earnings (as distinguished from its taxable income) for 1936, the year in which it is contended the deficits were transferred to Honolulu upon the liquidation of its subsidiaries.[2]

4. The Court erred in assuming that it is necessary for appellant to prove what portion of the deficits of the subsidiaries occurred in the tax year 1936. It is obvious—in fact it is stipulated (R. 33)—that the loss of $1,225,908.63 actually realized by Honolulu upon the liquidation of the subsidiaries occurred and could only occur at the moment the subsidiaries were liquidated on August 31, 1936, at which time Honolulu received all the assets of the subsidiaries in exchange for all the stock of the subsidiaries. Honolulu's earnings for 1936 available for dividends were actually eliminated by this loss. (R. 38.) Since the loss realized on this exchange exceeded Honolulu's earnings avail-

[2]That well-known text writers agree with appellant's position, that this Court has misconceived the question involved in this case, see Appendix "A".

able for dividends, the *excess* became an operating deficit of Honolulu, *and a 1936 operating deficit.* If this Court should hold that the principle of the *Sansome* case applies not only to inherited earnings, but also to inherited operating deficits, then it is equally obvious that this inheritance occurs and can only occur at the moment of liquidation. At that moment the entire accumulated operating deficits of the subsidiaries in the amount of $1,205,451.61 would be absorbed by Honolulu, with the result that the earnings available for dividends would be eliminated *in exactly the same manner as they actually were eliminated* by the loss sustained. Since these accumulated operating deficits exceeded Honolulu's earnings available for dividends, the *excess*[3] would become an operating deficit of Honolulu at that moment, *and necessarily a 1936 operating deficit of Honolulu.* Not only is this the obvious result; it is the only result which does not have absurd consequences. (See Appellant's Reply Brief, pp. 12-15.) It is therefore immaterial when the deficits were incurred by the subsidiaries. To consider this point material and to attribute the deficits of the subsidiaries to the parent corporation *for the years in which they were incurred by the subsidiaries* is to disregard the separate corporate entities of the subsidiaries during the years prior to the year of liquidation. (Appellant's Reply Brief, pp. 12-15.) Such a disregard of the separate corporate entities would be contrary to all the authorities.

---

[3]The operating deficits *of the subsidiaries* do not as such become operating deficits *of Honolulu.* It is important to note that it is only the *excess* of such deficits over Honolulu's earnings which becomes an operating deficit *of Honolulu.*

Wherefore, appellant respectfully urges that a rehearing may be granted and that the mandate of this Court may be stayed pending the disposition of this petition.

Dated, San Francisco, California,
February 20, 1945.

Respectfully submitted,
LEON DE FREMERY,
MORRISON, HOHFELD, FOERSTER,
SHUMAN & CLARK,
Attorneys for Appellant and Petitioner.

CERTIFICATE OF COUNSEL.

I hereby certify that I am of counsel for appellant and petitioner in the above entitled action and that in my judgment the foregoing petition for rehearing is well founded and that it is not interposed for delay.

Dated, San Francisco, California,
February 20, 1945.

LEON DE FREMERY,
Of Counsel for Appellant and Petitioner.

(Appendix "A" Follows.)

Appendix "A"

Appendix "A"

Appellant has just now been informed that Volume 1 of the Cyclopedic Tax Service* which is now in the process of being reprinted contains a statement relating to the decision of the District Court in the instant case. Paragraph 105.30 of this publication is entitled "Effect of Transferred 'Earnings or Profits' of a Predecessor or Transferor Corporation". After setting forth the principle of inherited earnings and profits under the doctrine of the *Sansome* case and the various situations to which this principle has been applied the text contains the following statement:

> "* * * it would seem by parity of reasoning that operating deficits of the predecessors should decrease the earnings and profits of the successor. The only case on this point which has been discovered is an unreported decision in Lorin A. Cranson v. U.S. (USDC, Calif., 1943), now pending on appeal to the Ninth Circuit, wherein it was held that the operating losses of several subsidiaries absorbed by the parent in a non-recognized liquidation under the equivalent of I.R.C., Sec. 112 (b) (6), did not decrease the earnings and profits of the parent. The District Court cites no authorities and gives no reasons for this holding."

*This is a recognized tax service of wide distribution published by the Coordinators' Corporation of Chicago. William KixMiller, President of Coordinators' Corporation, and Arnold R. Baar, Chief Legal and Editorial Adviser, have long been well known in the tax field. They were the founders and owners until recently of Commerce Clearing House whose Federal Income Tax Service was the first in the field and is one of the two leading services today.

Appellant has also been informed that at the time of the distribution of reprinted Volume 1 of this service it will be accompanied by an "As We Go To Press" section which will contain the following comment upon the affirmance of the District Court decision by this Court:

> "§105.30. Effect of Transferred 'Earnings or Profits' of a Predecessor or Transferor Corporation.
>
> Lorin A. Cranson v. U. S., ... F.(2d) ..... (CCA 9th, Jan. 24, 1945), aff'g USDC, Calif.
>
> "Since a corporation inherits the earnings and profits of a predecessor corporation acquired upon a tax-free exchange, it should follow, as stated in the text, that an operating deficit should also be inherited so as to decrease the earnings and profits of the successor. The only case in point is the Cranson decision which has now been affirmed by the Ninth Circuit.
>
> "As stated in the text, the lower court gave no reasons for its decision. The Appellate Court likewise gives no reasons, its opinion showing a complete misunderstanding of the issue. The opinion states:
>
> " 'This is an open question. If Honolulu (the successor corporation) itself had at the beginning of 1936 the same operating deficit, the deficit could not have been deducted. Long Beach Improvement Co. v. C.I.R., 5 BTA 590; Foley Securities Corporation v. C.I.R., 38 BTA 1036. An operating deficit is a bookkeeping convenience, which enables an individual to determine at a glance the present financial position of his business * * *'

"The two decisions cited by the Court (the only authorities referred to in the entire opinion) have no bearing on the problem involved. The Long Beach Improvement case holds, in the absence of a net operating loss carry-over provision in the law, that a corporation cannot deduct from its 1920 income a 1919 operating loss. The problem is not one of a deductible loss by the corporation, but of the amount of its accumulated earnings and profits available for dividends.

"The Foley Securities case, if relevant at all, is authority in favor of the taxpayer as it holds, for purposes of the dividends-paid credit of a personal holding company, that there can be no accumulated earnings and profits until an operating deficit is made good.

"As the Cranson decision is based upon a misapprehension of the problem involved, it cannot be considered a reliable precedent."

No. 10,644

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

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Appellant,

vs.

THE UNITED STATES OF AMERICA,

Appellee.

On Appeal from the District Court of the United States for the Northern District of California, Southern Division.

BRIEF FOR APPELLEE.

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PERNAU-WALSH PRINTING CO., SAN FRANCISCO

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On Appeal from the District Court of the United States for the Northern District of California, Southern Division.

BRIEF FOR APPELLEE.

OPINION BELOW.

The District Court rendered no opinion.

JURISDICTION.

This appeal involves federal income taxes for the calendar year 1936 in the amount of $51.84. The taxes in dispute were paid in equal installments on or about March 13, 1937, June 14, 1937, September 8, 1937 and December 15, 1937. (R. 3, 24, 28.) A deficiency of $9.21 was assessed and paid in two installments on March 25 and April 18, 1938. (R. 29.) A first amended claim for refund was filed on March 7, 1940 (R. 29),

and was rejected by letter dated July 22, 1941 (R. 30). On May 17, 1941, a second amended claim for refund was filed (R. 30), and was rejected by letter dated February 10, 1942 (R. 31, 57). Within the time provided in Section 3772 of the Internal Revenue Code and on April 22, 1942 (R. 23), the taxpayer brought an action in the District Court for the recovery of a portion of the taxes paid for the calendar year 1936 (R. 2-23). Jurisdiction was conferred on the District Court by Section 24, Twentieth, of the Judicial Code. The judgment was entered on October 25, 1943. (R. 62.) Within three months and on November 18, 1943, a notice of appeal was filed (R. 63), pursuant to the provisions of Section 128(a) of the Judicial Code, as amended.

QUESTIONS PRESENTED.

1. Whether the accumulated operating deficits of three wholly owned subsidiaries as of the date of their non-taxable liquidation in 1936, in the aggregate amount of $1,205,451.61, were absorbed by Honolulu Oil Corporation, Ltd., the parent corporation, thus resulting in a reduction of the earnings of Honolulu Oil Corporation, Ltd., otherwise available for dividends; or, in the alternative, whether the loss realized by Honolulu Oil Corporation, Ltd., upon the non-taxable liquidation of the wholly owned subsidiaries in 1936, in the amount of $1,225,908.63, reduced the earnings of Honolulu Oil Corporation, Ltd., available for dividends.

2. Whether the retroactive provisions of Section 501 of the Second Revenue Act of 1940, which section amends Section 115 of the Internal Revenue Code, violate the due process clause of the Fifth Amendment of the Constitution.

STATUTES AND REGULATIONS INVOLVED.

The statutes and regulations involved are set forth in the Appendix, *infra,* pp. i-vii.

STATEMENT.

The taxpayer sued to recover individual income taxes paid for the year 1936 in the amount of $51.84, plus statutory interest thereon. The sole issue involved in the case is the extent to which a distribution of $450.00 received by the taxpayer from the Honolulu Oil Corporation, Ltd., hereinafter referred to as "Honolulu", constituted a taxable dividend.

The case was tried solely on the pleadings and a stipulation of facts. The court below adopted the stipulation of facts as its findings of facts. (R. 60.) The pertinent stipulated facts are briefly as follows:

On August 31, 1936, Honolulu liquidated three wholly owned subsidiaries, hereinafter referred to as "subsidiaries", and took over all their assets subject to their liabilities. These liquidations constituted nontaxable transactions under Section 112(b) (6) of the Revenue Act of 1936. (R. 33.) Each of the subsidi-

aries sustained operating losses during the period from its operations, 1928 to 1933, inclusive, and as a result thereof they had an aggregate accumulated operating deficit of $1,205,451.61 as of the date of dissolution. (R. 36-37.)

These operating deficits included those sustained by the subsidiaries for January 1, 1936, to August 31, 1936. (R. 36.)

On January 1, 1936, Honolulu had available for dividends, earnings or profits accumulated since February 28, 1913, in the amount of $139,631.26. (R. 38.) In the liquidations Honolulu sustained a loss of $1,225,908.63 in the year 1936. (R. 33.) Honolulu's earnings or profits of the taxable year 1936 amounted to $931,553.82. (R. 38.) During the year 1936, Honolulu paid $1 per share dividend on each of its 937,743 shares of stock (R. 38), of which the taxpayer received $450 (R. 28-29).

By filing consolidated returns Honolulu had the tax benefit of the full amount of the operating losses of the subsidiaries for all pertinent years except 1933. (R. 37-38.)

SUMMARY OF ARGUMENT.

The operating deficits of the subsidiaries of Honolulu as of the date of their non-taxable liquidation in 1936 did not diminish the earnings or profits of Honolulu otherwise available for dividends in 1936 for the reason that the Congress in enacting Section 115 of the Revenue Act of 1936, and the Commissioner

of Internal Revenue in promulgating Article 115-3 of Treasury Regulations 94 dealt only with earnings or profits of transferor corporations. To construe Section 115 as dealing with operating deficits which the section does not mention, would be making a judicial addition to the language of the statute. But even if the surplus of Honolulu as of the beginning of the year 1936 were reduced by such deficits, Section 115(a) provides that dividends may be paid out of earnings or profits accumulated after February 28, 1913, or out of earnings or profits of the taxable year. These were more than sufficient to pay the dividends distributed by Honolulu during the year 1936.

The loss sustained by Honolulu upon the non-taxable liquidation of the subsidiaries did not diminish the earnings and profits of Honolulu available for dividends in 1936 for the same reasons that the operating deficits of the subsidiaries did not diminish the earnings of Honolulu otherwise available for dividends and for the further reason that Section 115(1) of the Internal Revenue Code was made applicable to the Revenue Act of 1936 by Section 501(c) of the Second Revenue Act of 1940. Section 115(1) provides that gain or loss realized on a transaction such as the one involved here, increases or decreases earnings or profits of a transferee corporation to, but not beyoud, the extent to which such realized gain or loss was *recognized* in computing net income under the law applicable to the year in which such sale or disposition was made. The word realized as used

in the section has reference to realized gains or losses which are recognized for income tax purposes such as a complete liquidation under Section 112(b) of the Revenue Act of 1936 in which no gain or loss is *"recognized."* This is clearly shown to be the construction placed on Section 115 by Congress as shown by S. Rep. No. 2114, 76th Cong., 3d Sess., p. 25.

The retroactive application of Section 501, Second Revenue Act of 1940, does not violate the due process clause of the Fifth Amendment of the Constitution when applied here. The taxpayer has not shown that he has been hurt by the retroactive application of the section, hence, he may not challenge its constitutionality. If it is retroactive there is abundant authority to the effect that retroactive legislation applied to Revenue Acts is not violative of the Fifth Amendment. There is doubt as to whether Section 501 is retroactive or was simply an explanation or a clarifying enactment explaining and clarifying existing law including the applicable sections of the Revenue Act of 1936.

ARGUMENT.

I.

THE OPERATING DEFICITS OF THE SUBSIDIARIES AS OF THE DATE OF THEIR NON-TAXABLE LIQUIDATION DID NOT DIMINISH THE EARNINGS OR PROFITS OF HONOLULU OTHERWISE AVAILABLE FOR DIVIDENDS.

The taxpayer contends first that the operating deficits of the aforesaid subsidiaries as of August 31,

1936, the date of their liquidation, in the aggregate amount of $1,205,451.61, were absorbed by Honolulu upon the non-taxable liquidation of the subsidiaries, and diminished earnings available for dividends (Br. 9-30); or, in the alternative, that the loss sustained by Honolulu upon the liquidation of the subsidiaries on August 31, 1936, in the amount of $1,225,908.63, reduced the earnings of Honolulu available for dividends (Br. 31-34).

In support of his first contention the taxpayer is relying on the doctrine, which was first enunciated in *Commissioner v. Sansome,* 60 F. 2d 931, 933 (C.C.A. 2d), certiorari denied, 287 U. S. 667, and consistently followed by this Court and other courts. See *United States v. Kauffman,* 62 F. 2d 1045. (C.C.A. 9th.) The principle established by the decisions in those cases is that a tax free exchange, pursuant to a reorganization, does not operate to "break the continuity of the corporate life," and that, when a reorganization "does not toll the company's life as continued venture", the earnings or profits of the transferor corporation are transferred intact over to the transferee corporation and shall be considered to be earnings or profits of the transferee corporation for taxable dividend purposes. There are no decisions to the contrary. Neither the *Sansome* nor the *Kauffman* case dealt with a liquidation of a subsidiary (which obviously does "toll" the corporation's life), but Article 115-11 of Regulations 94 nevertheless recognized that the same rule applies where there is a tax-free liquidation of a subsidiary.

It is the Government's position that the aforesaid doctrine is not controlling in the instant case for the reason that all of the cases in which this doctrine was applied, dealt only with net earnings or profits of transferor corporations. This doctrine was embodied in Section 115(c) (h) of the Revenue Act of 1936 (Appendix, *infra*). It may be noted that the statute and Regulations 94, Articles 115-3 and 115-11 (Appendix, *infra*) deal only with "earnings and profits" and make no mention of operating deficits. No decided cases have been found which involved facts analogous to those presented in the instant cases, *i.e.,* cases where transferor corporations had a net operating deficit at the time they transferred their assets and liabilities to a transferee corporation, and it has been the consistent Bureau of Internal Revenue practice to disregard operating deficits in cases of this nature on the ground that neither the Revenue Acts nor the Regulations provide for diminishing surplus by such operating deficits.

The provisions of the Revenue Act of 1936, dealing with distributions in connection with reorganizations are embodied in Section 115(c) and (h) (Appendix, *infra.*) A change in Section 115(h), from the corresponding section of the Revenue Act of 1934 is explained in S. Rep. No. 2156, 74th Cong., 2d Sess., p. 19 (1939-1 Cum. Bull. (Part 2) 678, 690), as follows:

> The rule, under existing law, with respect to the effect on corporate earnings or profits of a distribution which, under the applicable tax law,

is a non-taxable stock dividend or a distribution of stock or other exchange, on which gain is not recognized in full, is that such earnings or profits are not diminished by such distribution. In such cases, earnings or profits remain intact and hence available for distribution as dividends by the corporation making such distribution, or by another corporation to which the earnings or profits are transferred upon such reorganization or other change. This rule is stated only in part in Section 115(h) of the Revenue Act of 1934, and corresponding provisions of prior acts, but is the rule which is applied by the Treasury and supported by the courts in *Commissioner v. Sansome,* 60 Fed. (2) 931; *U. S. v. Kauffman,* 62 Fed. (2) 1045; *Murcheson v. Commissioner,* 76 Fed. (2) 641. While making no change in the rule as applied under existing law, the recommended amendment *is desirable in the interest of greater clarity.* (Italics supplied.)

Approval of that rule was again expressed in S. Rep. No. 2114, 76th Cong., 3d Sess., p. 25, dealing with Section 501 of the Second Revenue Act of 1940, in the following language:

> Under various provisions of the Internal Revenue Code dealing with exchanges and liquidations, the transfer of the property by a corporation to another corporation results in the non-recognition, in whole or in part, of the gain or loss realized by the transferor upon such transfer. *In such cases well established principles of income tax law require that the earnings and profits of the transferor shall go over to the transferee and shall be considered to be earnings*

> *and profits of the transferee for tax purposes.* These principles are to be given full effect under section 501, I.R.C. *The requirement of section 501 that there shall be no increase or decrease in earnings and profits by reason of a wholly unrecognized gain or loss is but another aspect of the principle under which the earnings and profits of the transferor become by reason of the transfer the earnings and profits of the transferee.* [Italics supplied.]

Thus both as to reorganizations and liquidations, Congress has never asserted that the provisions of Section 115 (a), (c) or (h) are designed to permit the successor corporation to deduct the deficits of its predecessor in determining its earnings or profits. It is well settled that in the construction of a law, its meaning must first be sought in the language employed by the lawmaker (*United States v. Goldenberg,* 168 U. S. 95, 103; *United States v. Standard Brewery,* 251 U. S. 210, 217); and it is clear from the foregoing that Section 115 of the Revenue Act of 1936 neither provides for, nor was it the intent of Congress that it should provide for diminishing the surplus of a transferee corporation by operating deficits of a transferor corporation in a liquidation under Section 112 (b) (6) (Appendix, *infra*). As said in *United States v. Standard Brewery, supra* (p. 217):

> If that language be plain, it is the duty of the courts to enforce the law as written, provided it be within the constitutional authority of the legislative body, which passed it. *Lake County v. Rollins,* 130 U. S. 662, 670, 671; *Bate Refrigerat-*

ing Co. v. Sulzberger, 157 U. S. 1, 33; *United States v. First National Bank.* 234 U. S. 245, 258; *Caminetti v. United States,* 242 U. S. 470, 485.
* * *

In *United States v. Goldenberg, supra,* the Court said (p. 103):

> *No mere omission, no mere failure to provide for contingencies, which it may seem wise to have specifically provided for, justify any judicial addition to the language of the statute.* * * * [Italics supplied.]

To hold that a corporation having surplus and earnings of its own in a sufficient amount to cover a distribution to its stockholders has not made a distribution of earnings and profits taxable to them because its predecessor has had an operating deficit, is in substance to hold that an exemption from income tax has been granted to the stockholders to that extent. Exemptions from taxation are never lightly to be inferred (*Heiner v. Colonial Trust Co.,* 275 U. S. 232), and will not be applied to a particular case unless granted to plain terms. *Denman v. Slayton,* 282 U. S. 514; *Anderson v. United States* 65 F. 2d 870 (C.C.A.8th). See also *Co-operative Oil Ass'n v. Commissioner,* 115 F. 2d 666 (C.C.A. 9th).

It is clear that Article 115-11 of Regulations 94 does not construe the *Sansome* principle as being applicable to deficits, even in the case of reorganizations. Nor do subsequent Regulations differ in this particular respect. Section 115(c) and (h) has also been reenacted in all subsequent Acts without any

substantial changes that would affect this question. Therefore, under "the familiar rule that a construction made by the body charged with the enforcement of a statute, which construction has long obtained in practical execution, and has been impliedly sanctioned by the reenactment of the statute without alteration in the particulars construed, when not plainly erroneous, must be treated as read into the statute." *New Haven R.R. v. Interstate Com. Com.,* 200 U. S. 361, 401-402. See also *Mass. Mutual Life Ins. Co. v. United States,* 288 U. S. 269, 273, where the court said:

> The Congress in the Revenue Acts of 1928 and 1932 reenacted section 245 without alteration. This action was taken with knowledge of the construction placed upon the section by the official charged with its administration. If the legislative body had considered the Treasury interpretation erroneous, it would have amended the section. Its failure so to do requires the conclusion that the regulation was not inconsistent with the intent of the statute * * *.

It is submitted that the Government's position with regard to the taxpayer's first contention is amply supported by the statute, Regulations and authorities mentioned above.

In this connection attention is invited to the fact that if the Court should hold, as taxpayer contends, that the doctrine in *Commissioner v. Sansome, supra,* should operate, not only in case of earnings or profits, but likewise where operating deficits are involved, then, under the specific provisions of Section 115(a)(2) of the Revenue Act of 1936, a very small

portion of the $937,430 dividends paid by Honolulu in the year 1936 could possibly constitute non-taxable dividends to the recipients thereof, for the reason that Section 115(a) contains an important provision which first appeared in that Act, to wit, that a dividend means any distribution:

> (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distribution made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.

This change in the 1936 Act is explained in S. Rep. No. 2156, 76th Cong., 2d Sess., p. 18 (1939-1 Cum. Bull. (Part 2) 678, 690), as follows:

> In order to enable corporations without regard to deficits existing at the beginning of the taxable year to obtain the benefit of the dividends paid credit for the purposes of the undistributed profits surtax, section 115(a) changes the definition of a dividend so as to include *distributions out of the earnings or profits of the current taxable year.* The amendment simplifies the determination by providing that distributions during the year, *not exceeding in amount the current earnings, are dividends constituting taxable income to the shareholder* and a dividends paid credit to the corporation. As respects such dividends the complicated determination of accumulated earnings or profits is rendered unnecessary. [Italics supplied.]

Furthermore, the decision in *Commissioner v. Sansome, supra,* p. 933, rationalizes that a tax free ex-

change does not operate to "break the continuity of the corporate life," and that, therefore, when a reorganization "does not toll the company's life as continued venture," the earnings of the "original, or subsidiary, company remain * * * 'earnings or profits' of the successor, or parent." The taxpayer has not shown the amounts of the operating deficits of the subsidiaries for the period January 1, to August 31, 1936. But those are the only deficits that on any theory could be material in determining earnings or profits of the taxable year. Honolulu can not deduct its own deficits for prior years and, obviously can not deduct those of another corporation.

The bookkeeping illustrations shown at pages 20-22 of taxpayer's brief are not helpful. They may illustrate "an historical record of a corporation's annual profits and losses" (Br. 21) and may also be one of the accepted methods used by bookkeepers in setting up the earned surplus account but they obviously do not show the entire picture from the income tax standpoint. For instance, they do not show "the earnings and profits of the taxable year" as contemplated by Section 115(a)(2) of the Revenue Act of 1936 and Article 115-3 of the Regulations; and they do not show that Honolulu received net assets of $464,714.63 from the liquidation (R. 59) and had received tax benefits in reduction of its net income for each of the years 1928 to 1933, inclusive, in the aggregate amount of $694,151.15 (R. 37, 38).

Likewise the Government does not agree with the taxpayer's reasoning on page 24 of his brief that

since an "operating deficit" in bookkeeping is but "a negative balance in the earned surplus account" the words "earnings and profits" as used in the statute and regulations should be interpreted to include "operating deficits." Each is the very antithesis of the other.

II.

THE LOSS SUSTAINED BY HONOLULU UPON THE NON-TAXABLE LIQUIDATION OF THE SUBSIDIARIES DID NOT DIMINISH THE EARNINGS OR PROFITS OF HONOLULU AVAILABLE FOR DIVIDENDS IN 1936.

The above is the converse of the taxpayer's alternative contention.

For income tax purposes Honolulu's investment in stocks of the subsidiaries at the date of liquidation must be reduced by $694,151.15, the amount of the subsidiaries' operating losses which was availed of to reduce the taxable income of the affiliated group in the years 1928 to 1932, inclusive. (R. 37, 38.) *Ilfeld Co. v. Hernandez,* 292 U.S. 62; *McLaughlin v. Lumber Co.,* 293 U.S. 351, 355, 357; *Inter-Island Steam Navigation, Ltd. v. Commissioner,* 42 B.T.A. 1064, 1073, 1074. The rationale of these cases is that a taxpayer having subtracted from income its losses in prior years cannot in subsequent years again deduct the losses directly or indirectly for tax purposes. Consequently, Honolulu's unrecovered investment in the stock of the subsidiaries was $531,755.48 ($1,225,906.63 less $694,151.15) instead of $1,225,906.63. (R. 33, 38.)

Whatever the amount of that loss, however, it is not deductible either in whole or in part because of the express language of Section 501 of the Revenue Act of 1940, adding subsection (1) to Section 115 of the Internal Revenue Code (Appendix, *infra*), and similarly amending all of the earlier revenue acts. Section 501(c) of that Act makes the amendment effective under each prior revenue act as if a part of such Act as of the date of its enactment. In so far as it is material here, it provides that the gain or loss realized by a corporation from the disposition of property increases or decreases its earnings or profits "to, but not beyond, the extent to which such a realized gain or loss was recognized in computing net income under the law applicable to the year in which such a sale or disposition was made." The Government had always contended that this was a correct construction of earlier statutes but had lost some of these cases and by Section 501 of the Revenue Act of 1940 Congress specifically endorsed and confirmed the Commissioner's position.[1]

As used in this provision of the law, the term "recognized" has reference to the realized gain or loss which was recognized for income tax purposes by the statute applicable to the year in which the transaction occurred. Where no gain or loss was recognized for tax purposes, as in this case, because of the provi-

[1]See H. Rep. 2894, 76th Cong., 3rd Sess., p. 41 (1940-2 Cum. Bull. 496, 526). The report specifically refers to the case of *Commissioner v. F. J. Young Corp.*, 103 F. 2d 137 (C.C.A. 3d), as one of the cases which had reached a contrary conclusion. See also *Elmhurst v. Commissioner*, 41 B.T.A. 348.

sions of Section 112(b)(6) (Appendix, *infra*), the gain or loss realized by the corporation has no effect upon the computation of earnings or profits under Section 115. See Section 29.115-11 of Regulations 111, promulgated under the Internal Revenue Code, as amended by T. D. 5304, 1943-22 Internal Revenue Bulletin 18.

This provision of the law plainly prevents the reduction of the earnings or profits of Honolulu by the amount of its unrecovered investment in stocks of the liquidated subsidiaries. There can be no question but that the statute applies[2] and if there were such a doubt, it would be removed by the fact that the Senate Report specifically refers to this situation. See S. Rep. No. 2114, 76th Cong., 3rd Sess., p. 25 (1940-2 Cum. Bull. 528, 546-547).

III.

THE RETROACTIVE APPLICATION OF SECTION 501, SECOND REVENUE ACT OF 1940, DOES NOT VIOLATE THE DUE PROCESS CLAUSE OF THE FIFTH AMENDMENT OF THE CONSTITUTION WHEN APPLIED HERE.

The taxpayer argues that to apply the provisions of Section 501 of the Revenue Act of 1940 to a determination of the taxable statute of distributions made by Honolulu in 1936 violates the due process clause of the Fifth Amendment. The argument as-

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[2]This case was not pending before the District Court on October 8, 1940, the effective date of the Second Revenue Act of 1940, so that the proviso contained in Section 501(c), permitting the Board of Tax Appeals and the courts to dispose of pending cases without regard to this provision, has no application.

sumes that Section 501 is a new and retroactive law. The Committee Reports, however, show that the purpose of Congress was to clarify existing law, eliminating all controversy as to the meaning of earnings and profits in the Internal Revenue Code and the previous revenue acts. H. Rep· No. 2894, *supra.* Despite adverse decisions, the Commissioner had never ceased to urge that only to the extent that gains or losses were recognized for tax purposes should they figure in the computation of the earnings and profits of the corporation for dividend purposes. See Article 115-3 of Regulation 94, Appendix, *infra.* It is clear, therefore, that neither Honolulu nor the taxpayer had any basis for any assumption in 1936 that part of the dividends here involved would be tax exempt because Honolulu's loss on the liquidation of its subsidiaries would reduce the earnings or profits available for dividend distribution. Nor has the taxpayer shown that either made such an assumption or that no distribution would have been made except on such an assumption. Neither has been the victim of any injustice or has been hurt by the retroactive application of the statute and they have no standing to attack the constitutionality of Section 501 on the ground of objectionable retroactivity. See *Wilgard Realty Co. v. Commissioner,* 127 F. 2d 514, 517 (C.C.A. 2d).

But even if the legislation had been genuinely retroactive legislation rather than clarifying legislation, that would not serve to establish that the provision was unconstitutional. The taxpayers have cited

no case in which an income tax law has been invalid on the ground of objectionable retroactivity and we know of none. On the contrary, there are many decisions holding that retroactive provisions of income tax laws are valid. *Cooper v. United States,* 280 U. S. 409; *United States v. Hudson,* 299 U. S. 498; *Welch v. Henry,* 305 U. S. 134; *Martz v. Commissioner,* 82 F. 2d 110 (C.C.A. 9th); *Wilgard Realty Co. v. Commissioner, supra; Commissioner v. Corpus Christi T. Co.,* 126 F. 2d 898 (C.C.A. 5th); *D. W. Klein Co. v. Commissioner,* 123 F. 2d 871 (C.C.A. 7th), certiorari denied, 315 U. S. 819. The *Wilgard Realty Co.* case and the *D. W. Klein* case involving a retroactive amendment enacted in 1939 were held valid as applied to transactions occurring in 1932. See also *Commissioner v. Corpus Christi T. Co., supra.*

The Supreme Court said in *Welch v. Henry, supra,* speaking by Justice Stone,[3] now Chief Justice (pp. 146, 149):

> * * * a tax is not necessarily unconstitutional because retroactive. * * *
>
> * * * * * * *
>
> The contention that the retroactive application of the Revenue Acts is a denial of the due process guaranteed by the Fifth Amendment has been uniformly rejected. [Many cases cited.]

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[3]Although three Justices dissented from the conclusion of the majority in *Welch v. Henry,* supra, that the particular retroactive Wisconsin legislation was valid, the dissenters explicitly recognized (p. 154) that a retroactive "revision of an existing general income tax system theretofore in force" would be constitutional.

A similar contention was rejected in the case of *Wheeler v. Commissioner,* 1 T. C. 640, 645, now pending before this Court. The Tax Court held that the Congress clearly intended Section 501 of the Second Revenue Act of 1940 to apply to transactions in prior years and that such application is not unconstitutional as "in violation of the due process clause of the Fifth Amendment to the Constitution."

CONCLUSION.

The decision of the court below is correct and should, accordingly, be affirmed.

Dated, March 24, 1944.

Respectfully submitted,

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(Appendix Follows.)

Appendix.

Appendix

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. In the case of Presidents of the United States and judges of courts of the United States taking office after June 6, 1932, the compensation received as such shall be included in gross income; and all Acts fixing the compensation of such Presidents and judges are hereby amended accordingly.

SEC. 112. RECOGNITION OF GAIN OR LOSS.

* * * * * * *

(b) *Exchanges Solely in Kind.*—

* * * * * * *

(6) *Property Received by Corporation on Complete Liquidation of Another.*—No gain or loss shall be recognized upon the receipt by a corporation of property distributed in complete liquidation of another corporation. * * *

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(a) *Definition of Dividend.*—The term "dividend" when used in this title (except in section 203(a)(3) and section 207(c)(1), relating to insurance companies) means any distribution made by a corporation to its shareholders, whether in money or in other property (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.

* * * * * * *

(c) *Distribution in Liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as a part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. Despite the provisions of section 117(a), 100 per centum of the gain so recognized shall be taken into account in computing net income, except in the case of amounts distributed in complete liquidation of a corporation. For the purpose of the preceding sentence, "complete liquidation" includes any one of a series of distributions made by a corporation in complete cancellation or redemption of all of its stock in accordance with a bona fide plan of

liquidation and under which the transfer of the property under the liquidation is to be completed within a time specified in the plan, not exceeding two years from the close of the taxable year during which is made the first of the series of distributions under the plan. In the case of amounts distributed (whether before January 1, 1934, or on or after such date) in partial liquidation (other than a distribution within the provisions of subsection (h) of this section of stock or securities in connection with a reorganization) the part of such distribution which is properly chargeable to capital account shall not be considered a distribution of earnings or profits.

* * * * * * *

(h) *Effect on earnings and Profits of Distributions of Stock.*.—The distribution (whether before January 1, 1936, or on or after such date) to a distributee by or on behalf of a corporation of its stock or securities or stock or securities in another corporation shall not be considered a distribution of earnings or profits of any corporation.—

(1) if no gain to such distributee from the receipt of such stock or securities was recognized by law, or

(2) if the distribution was not subject to tax in the hands of such distributee because it did not constitute income to him within the meaning of the Sixteenth Amendment to the Constitution or because exempt to him under section 115(f) of the Revenue Act of 1934 or a corresponding provision of a prior Revenue Act.

* * * * * * *

Internal Revenue Code:

Sec. 115. [As amended by Section 501(a), Second Revenue Act of 1940, c. 757, 54 Stat. 974.] DISTRIBUTIONS BY CORPORATIONS.

* * * * * * *

(1) *Effect on earnings and profits of gain or loss and of receipt of tax-free distributions.*—The gain or loss realized from the sale or other disposition (after February 28, 1913) of property by a corporation—

* * * * * * *

(2) for the purpose of the computation of earnings and profits of the corporation for any period beginning after February 28, 1913, shall be determined by using as the adjusted basis the adjusted basis (under the law applicable to the year in which the sale or other disposition was made) for determining gain.

Gain or loss so realized shall increase or decrease the earnings and profits to, but not beyond, the extent to which such a realized gain or loss was recognized in computing net income under the law applicable to the year in which such sale or disposition was made. * * *

* * * * * * *

(26 U. S. C. 1940 ed., Sec. 115.)

Second Revenue Act of 1940, c. 757, 54 Stat. 974:

Sec. 501. EARNINGS AND PROFITS OF CORPORATIONS.

* * * * * * *

(c) *Under prior acts.*—For the purposes of the Revenue Act of 1938 or any prior Revenue

Act the amendments made to the Internal Revenue Code by subsection (a) of this section shall be effective as if they were a part of each such Revenue Act on the date of its enactment. Nothing in this subsection shall affect the tax liability of any taxpayer for any year which, on September 20, 1940, was pending before, or was therefore determined by, the Board of Tax Appeals, or any court of the United States.

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

Art. 115-3. *Earnings or Profits.*—In determining the amount of earnings or profits (whether of the taxable year, or accumulated since February 28, 1931, or accumulated prior to March 1, 1913) due consideration must be given to the facts, and mere bookkeeping entries increasing or decreasing surplus will not be conclusive.

Among the items entering into the computation of corporate earnings or profits for a particular period are all income exempted by statute, income not taxable by the Federal Government under the Constitution, as well as all items includible in gross income under Section 22(a) of the Act or corresponding provisions of prior Acts. Gain and losses within the purview of section 112 or corresponding provisions of prior Acts are brought into the earnings and profits at the time and to the extent such gains and losses are recognized under that section. * * *

Art. 115-11. *Effect on earnings or profits on certain tax-free exchanges and tax-free distributions.*—If under the law applicable to the year

in which any transfer or exchange of property after February 28, 1913, was made (including transfers in connection with a reorganization or a complete liquidation under section 112(b)(6) and intercompany transfers of property during a period of affiliation), gain or loss was not recognized (or was recognized only to the extent of the property received other than that permitted by such law to be received without the recognition of gain), then proper adjustment and allocation of the earnings or profits of the transferor shall be made as between the transferor and transferee corporations.

The general rule provided in section 115 (b) that every distribution is made out of earnings or profits to the extent thereof and from the most recently accumulated earnings or profits, does not apply to:

(1) The distribution, in pursuance of a plan of reorganization, by or on behalf of a corporation a party to the reorganization, to its shareholders of stock or securities in such corporation or in another corporation a party to the reorganization—

(A) in any taxable year beginning before January 1, 1934, without the surrender by the distributees of stock or securities in such corporation (see section 112(g) of the Revenue Act of 1932); or

(B) in any taxable year (beginning before January 1, 1936, or on or after such date) in exchange for its stock or securities (see section 112(b)(3))

if no gain to the distributees from the receipt of such stock or securities was recognized by law.

(2) A stock dividend which was not subject to tax in the hands of the distributee because either it did not constitute income to him within the meaning of the sixteenth amendment to the Constitution or because exempt to him under section 115(f) of the Revenue Act of 1934 or a corresponding provision of a prior Revenue Act.

A distribution described in paragraph (1) and (2) above does not diminish the earnings or profits of any corporation. In such cases, the earnings or profits remain intact and available for distribution as dividends by the corporation making such distribution, or by another corporation to which the earnings or profits are transferred upon such reorganization or other exchange.

For the purposes of this article, the terms "reorganization" and "party to the reorganization" shall, for any taxable year beginning before January 1, 1934, have the meanings assigned to such terms in section 112 of the Revenue Act of 1932, and for any taxable year beginning after December 31, 1933, and before January 1, 1936, have the meanings assigned to such terms in section 112 of the Revenue Act of 1934.

No. 10,644

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

LORIN A. CRANSON,
Appellant,

vs.

THE UNITED STATES OF AMERICA,
Appellee.

APPELLANT'S REPLY BRIEF.

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No. 10,644

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

LORIN A. CRANSON,
Appellant,

vs.

THE UNITED STATES OF AMERICA,
Appellee.

APPELLANT'S REPLY BRIEF.

I.

THE GOVERNMENT'S FIRST ARGUMENT, THAT THE OPERATING DEFICITS OF THE SUBSIDIARIES DID NOT DIMINISH THE EARNINGS OR PROFITS OF HONOLULU AVAILABLE FOR DIVIDENDS, IS BASED ON A MISCONCEPTION OF THE STATUTE.

The major portion of that part of the argument in appellant's opening brief relating to the absorption by Honolulu of the operating deficits of its subsidiaries was devoted to the proposition that no logical distinction can be drawn between the transfer of corporate earnings in a nontaxable reorganization and the transfer of operating deficits. The Government in its brief makes no attempt to refute this proposition, and it must therefore be presumed that the point is conceded and that it is admitted it is illogical for the Government to rule on the one hand that

corporate earnings are transferred in nontaxable reorganizations, as the Treasury Regulations provide, and on the other hand to deny, as it does in the instant case, that operating deficits must receive the same treatment.

We wish to emphasize at this point that not only is the Government's position illogical but it is inequitable as well, since it results in taxing as income that which in fact is not income. It is admitted that the dividends received by the stockholders of Honolulu in 1936 were *actually* distributions of capital.[1] Since the stockholders were actually receiving a return of their capital and not receiving income, they should not be subjected to tax unless the law clearly requires such a result. Such a result will be avoided if the Court holds that the doctrine of the *Sansome* case, i.e., that nontaxable reorganizations do not break the continuity of the corporate life as a continuing venture, applies to the transfer of operating deficits as well as to transfer of earnings or profits.

The Government's main argument in support of its illogical and inequitable position may be summarized as follows: Subsections (c) and (h) of section 115 of the Revenue Act of 1936 provide for the transfer of corporate earnings in nontaxable reorganizations (Br.

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[1]It is stipulated that Honolulu's earnings available for dividends on January 1, 1936, amounted to $139,631.26, that Honolulu's earnings during 1936, before giving any effect to the liquidation of the subsidiaries, amounted to $931,553.82 (R. 38), and that Honolulu realized a loss of $1,225,908.63 upon the liquidation of the subsidiaries in 1936 (R. 33). Since the loss exceeded the total earnings available, all dividends in 1936 were actually distributions of capital, except possibly to the small extent indicated in the footnote on page 6 of our opening brief.

p. 8, lines 5 and 6); the statute does not provide for the transfer of an operating deficit (Br. p. 8, lines 7-10); if the language of the statute is plain, it is the duty of the courts to enforce the law as written (Br. pp. 10-11); from which it is concluded that earnings alone are to be transferred and operating deficits not transferred. This argument is unsound. The fallacy lies in the fact that the major premise is false; subsections (c) and (h) of section 115 do *not* provide for the transfer of corporate earnings in a nontaxable reorganization.

(a) Subsections (c) and (h) of section 115, Revenue Act of 1936, do not provide for the transfer of corporate earnings in nontaxable reorganizations, and have no application to the instant case.

Section 115(c) is set forth in full in the appendix. Omitting the portions of this section relating to partial liquidation and defining "complete liquidation", neither of which can have any possible application, the remaining portion of this section of the statute reads as follows:

> "Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as a part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112."

The foregoing section of the statute relates to the taxation of liquidating dividends to the recipient.

There is obviously nothing in this section of the statute which remotely relates to the transfer of the earnings or profits of the predecessor corporation to the successor corporation in a nontaxable reorganization.

Section 115(h) has likewise no bearing whatever on the transfer of corporate earnings in nontaxable reorganizations. This section of the statute reads in full as follows:

> "(h) **Effect on earnings and profits of distributions of stock.**—The distribution (whether before January 1, 1936, or on or after such date) to a distributee by or on behalf of a corporation of its stock or securities or stock or securities in another corporation shall not be considered a distribution of earnings or profits of any corporation—
>
> (1) if no gain to such distributee from the receipt of such stock or securities was recognized by law, or
>
> (2) if the distribution was not subject to tax in the hands of such distributee because it did not constitute income to him within the meaning of the Sixteenth Amendment to the Constitution or because exempt to him under section 115 (f) of the Revenue Act of 1934 or a corresponding provision of a prior Revenue Act.
>
> As used in this subsection the term 'stock or securities' includes rights to acquire stock or securities."

Section 115(h) merely provides that the distribution by a corporation of its own stock or securities, or stock or securities of another corporation, shall

not be considered a distribution of earnings or profits if the distribution is not taxable to the recipient. The purpose of this section was to prevent a corporation from making a tax-free distribution to its stockholders of stock or securities, as in a merger or consolidation, and at the same time contend that it had reduced its earnings available for dividends.[2] It obviously has no bearing in the instant case, since neither the subsidiaries nor Honolulu made any distribution of stock or securities.

In referring to the doctrine of the *Sansome* and *Kauffman* cases, the Government makes the statement: "This doctrine was embodied in Section 115 (c) (h) of the Revenue Act of 1936." (Br. p. 8.) As we have seen, this statement is not correct and since it constitutes the major premise of the Government's argument that the doctrine of the *Sansome* case does not apply to operating deficits, the entire argument falls with its major premise.

(b) Failure of the statute to provide for the transfer of operating deficits is therefore of no significance.

There is no section of the Revenue Acts or the Internal Revenue Code which incorporates the doctrine of the Sansome Rule or otherwise deals with the transfer of corporate earnings in nontaxable reorganizations. The statements on page 8 of the Government's brief, and again on page 10, that the Revenue Acts do

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[2]Section 115(h) appeared in its original form as section 203(g) of the Revenue Act of 1924. The reasons for its enactment appear on page 9 of a statement prepared for the use of the Senate Committee on Finance (68th Congress, 1st Session), entitled "Statement of the Changes made in the Revenue Act of 1921 by H.R. 6715 and the Reasons Therefor."

not provide for the transfer of an operating deficit in corporate reorganizations, thus loses all significance, since the Revenue Acts likewise do not provide for the transfer of corporate earnings.

The references to the Sansome Rule contained in the extracts from the reports of the Senate Finance Committee contained on pages 8 to 10 of the Government's brief do not support the Government's position. The extract commencing on page 8 was written in explanation of section 115(h) of the Revenue Act of 1936, which, as we have heretofore pointed out (supra, pp. 4-5), has no bearing whatever on the questions involved in the instant case. The Committee Report explains that under section 115(h) earnings or profits are not reduced by a distribution of corporate securities in nontaxable reorganizations, adding the comment that such earnings remain available for distribution by the corporation making such distribution, or by another corporation to which the earnings or profits are transferred upon the reorganization. The latter part of this statement is a recognition of the Sansome Rule, but can in no sense be taken as even implying that the rule does not apply equally to operating deficits. This is so because corporations with operating deficits are obviously not affected by section 115(h), since such corporations have no earned surplus and this section was intended solely to prevent corporations from claiming that their earned surplus available for dividends had been decreased by distributions of stock or securities which were not taxable to the recipient.

The extract from the report of the Senate Finance

Committee commencing on page 9 of the Government's brief was written in explanation of section 501 of the Second Revenue Act of 1940, which relates to the *deduction of the loss* sustained by Honolulu upon the liquidation of its subsidiaries (this being the section which appellant contends is unconstitutional if applied in the instant case), and has no bearing upon the *transfer of the operating deficits* of the subsidiaries. The doctrine of the Sansome Rule is again referred to in this extract, but this cannot be taken as denying the application of the rule to operating deficits. In fact the last sentence of the extract, stating in part that the requirement of section 501 to the effect that there shall be no *decrease* in earnings and profits by reason of an unrecognized *loss* is but another aspect of the Sansome Rule, is at least an implication, if not a direct statement, that the rule *does* apply to operating deficits. To reduce earnings available for dividends by the loss realized, though not recognized for income tax purposes, on the liquidation of the subsidiaries, and also to allow the transfer of their operating deficits, would give a double effect to the same loss. Therefore the provision that the unrecognized loss does *not* reduce earnings can be correctly described as but another aspect of the Sansome Rule *only if the rule includes the transfer of operating deficits.*

In any event, no significance can be attached to the fact that a Committee of Congress in setting forth the doctrine of the *Sansome* case confines its statement to the doctrine as enunciated in the decided cases. The decided cases have dealt solely with earnings or profits and it is natural that the Committee report in re-

ferring to this doctrine should state it as set forth in those cases. Furthermore, the Committee's statement of the doctrine is not entitled to any weight, since, as we have stated, there is no section of the Revenue Acts which deals with this subject, and Committee reports are entitled to weight only when resorted to as an aid in statutory construction.

The same observations apply to the Treasury Regulations. The fact that these Regulations may contain a statement of the doctrine of the *Sansome* case, in so far as that doctrine has been enunciated by the courts, is of no significance in determining whether the doctrine also includes matters not yet covered by court decisions. The Government argues (Br. pp. 11-12) that the reenactment of subsections (c) and (h) of section 115 "without any substantial changes that would affect this question" must be given the effect of reading the statement contained in the Regulations into the statute. As we have seen (supra, pp. 3-5) subsections (c) and (h) of section 115 have no relation whatever to the doctrine of the *Sansome* case, and accordingly their reenactment without substantial change cannot possibly be considered an approval of the doctrine of that case as set forth in the Regulations.

One further point requires mention on this phase of the Government's argument. On page 11 of the Government's brief, it is argued that a decision in appellant's favor would amount in substance to the granting of an exemption from income tax to the stockholders of Honolulu Oil Corporation and cases are cited in support of the proposition that exemptions

from taxation are never lightly to be inferred and must be granted in plain terms. Of course, the stockholders are not claiming exemption from taxation but are claiming that the dividends paid by Honolulu were to a large extent capital distributions and therefore not income and not subject to tax.

Included in the cases cited on page 11, relating to exemption from taxation, the Government cites *Co-operative Oil Ass'n v. Commissioner,* 115 Fed. (2d) 666 (C.C.A. 9). This case does not relate to exemption from taxation but stands for the proposition that deductions from gross income in the determination of statutory net income subject to tax are statutory privileges allowed as a matter of grace and that a taxpayer seeking a deduction must find statutory warrant therefor. The Government advanced such an argument in the Court below and cited this case to support it, but has abandoned the argument here. Appellant is obviously not seeking a deduction from gross income but is contending that certain distributions received from Honolulu Oil Corporation are not income as defined by the statute but are capital distributions. Nor is it contended that Honolulu is entitled to a deduction from gross income. Statutory deductions apply only in the determination of statutory net income subject to tax and have no application to the determination of earnings available for dividends. Since the Government has abandoned the argument that appellant is seeking a deduction not provided for by statute, it erred in citing the *Co-operative Oil Ass'n* case.

It also erred in stating our contention to be that "the words 'earnings and profits' as used in the statute

* * * should be interpreted to include 'operating deficits' '' (Br. p. 15). We are not making any contention with respect to the meaning of any statutory provision. Here again the Government seems to persist in the error that the Sansome Rule is a statutory provision.

II.

THE GOVERNMENT ERRS IN ASSUMING THAT IF THE OPERATING DEFICITS OF THE SUBSIDIARIES ARE ABSORBED BY HONOLULU THEY WILL NOT REDUCE THE EARNINGS OR PROFITS OF THE TAXABLE YEAR.

The Government advances the argument (Br. pp. 12-14) that if the Court should hold that the Sansome Rule operates not only with respect to earnings or profits but likewise where operating deficits are involved, then the absorption of the operating deficits of the subsidiaries in 1936 will not reduce Honolulu's earnings for 1936. This argument is based on the assumption that section 115(a) of the Act of 1936 would prevent such a reduction. This section of the statute reads in full as follows:

> "(a) **Definition of Dividend.**—The term 'dividend' when used in this title (except in section 203 (a) (3) and section 207 (c) (1), relating to insurance companies) means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), with-

out regard to the amount of the earnings and profits at the time the distribution was made."

The portion of this section relied upon by the Government is that part defining a dividend to include any distribution "out of the earnings or profits of the taxable year". These words do not limit in any manner the *determination* of the earnings or profits of the taxable year, but merely state that any distribution therefrom constitutes a taxable dividend. If the loss actually realized by Honolulu on the liquidation of its subsidiaries in 1936 reduced its earnings available for dividends (as it would were it not for the retroactive provisions of section 501 of the Second Revenue Act of 1940 discussed elsewhere), it is clear that this loss, in the same manner as any other loss or deduction, would reduce Honolulu's earnings for 1936 available for dividends. If the Court should hold that the operating deficits of the subsidiaries are absorbed by Honolulu, then the loss on liquidation should of course not be allowed to reduce the earnings of Honolulu, since this would be giving a double effect to the same loss. Under such circumstances there could be no objection to the retroactive application of section 501 of the Second Revenue Act of 1940, which was apparently designed to prevent this double effect, and which would then operate in an equitable manner. If, then, the Court should hold that the operating deficits of the subsidiaries are absorbed by Honolulu, it is apparent that they would take the place of the loss on liquidation otherwise allowable as a reduction of the earnings of Honolulu. Since the loss on liquidation would, as we have seen, obviously reduce the earnings of

Honolulu for 1936, it is difficult to understand the Government's assumption that the transfer of the operating deficits would not have the same effect.

All 1936 transactions necessarily affect earnings for 1936, the balance of the profit or loss, as the case may be, at the end of the year being transferred to the earned surplus account. In order to demonstrate the fallacy of the Government's assumption that the operating deficits of the subsidiaries, *even though absorbed by Honolulu,* do not reduce its earnings for 1936, let us assume for the moment that this assumption is correct. If the earnings for 1936 are not reduced, the only possible alternative is that the earnings of Honolulu for prior years in which the losses were sustained by the subsidiaries must be reduced, since otherwise there would be no reduction whatever and the operating deficits could not have been absorbed by Honolulu. But taxes have been paid by the stockholders of Honolulu on these prior annual earnings without taking the annual operating deficits of the subsidiaries into account. The stockholders could not have avoided the payment of these taxes because to take the deficits of the subsidiaries into account would require a disregard of the separate corporate entities of the subsidiaries—a result which is not supported by any authority. Thus the Government is arguing for the proposition that the stockholders must pay taxes on the annual dividends for prior years without taking into account the losses of the subsidiaries, and at the same time that the earnings for 1936 are not reduced by these losses when transferred to the parent corporation, so that the stockholders *never* receive the

benefit of the reduction in earnings.

The error in the Government's assumption becomes more readily apparent if it be assumed that the subsidiaries had earnings rather than operating deficits. Suppose, for example, that Honolulu had incorporated a subsidiary in 1936, and that this subsidiary had earnings of $100,000 a year for the years 1936, 1937, 1938 and 1939. Assume that Honolulu had an operating deficit in the amount of $500,000 at the beginning of 1936, had yearly earnings of $1,000,000, and declared dividends of $1,100,000, in each of these years. Since the dividends of Honolulu in each of these years exceeded its earnings by $100,000, it follows that for this period of four years the stockholders of Honolulu will have received total capital distributions in the amount of $400,000. Assume further that in January, 1940, the subsidiary, which has an earned surplus of $400,000, liquidates, and that Honolulu has earnings of $1,000,000 in 1940, not taking into account the earned surplus of the subsidiary in the amount of $400,000 which was transferred to Honolulu under the Sansome Rule. Honolulu then declares total dividends of $1,400,000 in 1940. It will be of assistance to tabulate the foregoing figures as follows:

	HONOLULU			SUBSIDIARY
Year	Earnings	Dividends	Capital Distributions	Earnings
12/31/35	$ *500,000*			
1936	1,000,000	$1,100,000	$100,000	$100,000
1937	1,000,000	1,100,000	100,000	100,000
1938	1,000,000	1,100,000	100,000	100,000
1939	1,000,000	1,100,000	100,000	100,000
1940	1,000,000	1,400,000		

Since under the doctrine of the *Sansome* case the subsidiary's earnings in the amount of $400,000 had been transferred to Honolulu in 1940, it seems apparent that Honolulu's earnings for that year will be $1,400,000 and not $1,000,000 as the Government assumes. (This certainly would be the result if the subsidiary's earnings had been transferred by the declaration of a dividend immediately prior to liquidation.) But let us suppose for the moment that the Government is correct and that the transfer of the subsidiary's earnings did not increase Honolulu's earnings for 1940. In such case the stockholders of Honolulu, having received distributions of $1,400,000 in 1940, which according to the assumption exceeded the available earnings by $400,000, will have received further capital distributions in the amount of $400,000. Since they had previously received capital distributions for the years 1936 to 1939, inclusive, in the amount of $400,000, their total capital distributions would thus be $800,000. This is obviously erroneous, since Honolulu and its subsidiary combined earned during the five years 1936 to 1940, inclusive, a total of $5,400,000, and distributed to Honolulu's stockholders $5,800,000. Thus the total capital distributions are only $400,000. The Government could not correct this erroneous result by going back to the years 1936 to 1939 and disallowing the capital distributions of $100,000 in each of these years (which incidentally might be barred by the statute of limitations), because to contend that the earnings of the subsidiary in the amount of $100,000 in each year were available for

dividends by Honolulu disregards the separate corporate entities, which, as we have stated, is not supported by any authority.

It seems apparent, therefore, that the liquidation of a subsidiary and the transfer of its earnings to the parent corporation results in increasing the earnings of the parent corporation for the year in which the liquidation occurred. The transfer of an operating deficit would necessarily result in the same manner, that is, in the reduction of the earnings for the current taxable year. Thus earnings or operating deficits of the subsidiary for prior years are obviously not prior years' earnings or operating deficits of the parent, but upon transfer on the dissolution of the subsidiary become current earnings or operating deficits of the parent. As stated heretofore, all transactions necessarily affect the earnings of the year in which they occur. To hold otherwise in the case of the transfer of a subsidiary's earnings or operating deficits results in a disregard of the corporate entity, since the only possible alternative is to segregate the earnings and losses of the subsidiary into the respective years in which they occurred and assume a corresponding effect upon the earnings of the parent. Such a disregard of the separate corporate entities is not supported by any authority.

III.

THE GOVERNMENT ERRS IN REDUCING THE LOSS SUSTAINED BY HONOLULU UPON THE LIQUIDATION OF ITS SUBSIDIARIES BY THE AMOUNT OF THE SUBSIDIARIES' OPERATING LOSSES WHICH WERE AVAILED OF ON CONSOLIDATED RETURNS.

On page 15 of its brief the Government advances the argument that the amount of the loss sustained by Honolulu upon the liquidation of its subsidiaries must be reduced by the amount of $694,151.15, representing the amount of the subsidiaries' operating losses availed of to reduce the taxable income of the affiliated group in the years 1928 to 1932, inclusive. It is true that in order to prevent a double deduction for the purpose of determining *Honolulu's income taxes,* Honolulu's investment in the stock of its subsidiaries must be reduced by the amount of the losses of the subsidiaries which were utilized on a consolidated return to reduce Honolulu's income which would otherwise have been subject to tax. This means that in the event Honolulu had sold the stock of its subsidiaries or had attempted for tax purposes to deduct the loss on liquidation, its cost would have to be reduced by the amount of $694,151.15 in order to prevent a double deduction by Honolulu. However, the *earnings available for dividends* by Honolulu were not affected by the fact that it filed a consolidated return with its subsidiaries for income tax purposes. In so far as the determination of earnings available for dividends is concerned, Honolulu's cost remains unaffected by the fact that consolidated returns had been filed for tax purposes, and no part of the losses of the subsidiaries can reduce the

earnings of Honolulu, without completely disregarding the separate corporate entities, until the full loss is realized on ultimate liquidation. There is thus no double deduction. It is only in the determination of statutory net income for tax purposes that the basis of the stock of the subsidiaries to Honolulu is not their actual cost. The distinction between statutory net income and earnings available for dividends is fully set forth in subdivision II(a) of appellant's opening brief and need not be repeated here. The Government has evidently confused the determination of net income for tax purposes with the determination of earnings or profits available for dividends.

IV.

THE ATTEMPTED RETROACTIVE APPLICATION OF SECTION 501 OF THE SECOND REVENUE ACT OF 1940 VIOLATES THE DUE PROCESS CLAUSE OF THE CONSTITUTION.

The cases cited by the Government (Br. p. 19) in support of its argument that the retroactive application of section 501 of the Second Revenue Act of 1940 is not unconstitutional are readily distinguishable from the instant case. In *United States v. Hudson,* 299 U. S. 498, the statute upheld as constitutional had been made retroactive for a period of thirty-five days. In *Cooper v. United States,* 280 U. S. 409, and *Martz v. Commissioner,* 82 F. (2d) 110 (C.C.A. 9), the provisions upheld as constitutional had been given retroactive effect only to the beginning of the calendar year in which the statutes were enacted. The situation existing in the case of *Wilgard Realty Co. v. Commissioner,*

127 F. (2d) 514 (C.C.A. 2), clearly justified the retroactive application of the statute as pointed out in appellant's opening brief. The same statutory provision was involved in *Commissioner v. Corpus Christi Terminal Co.,* 126 F. (2d) 898 (C.C.A. 5), and *D. W. Klein Co. v. Commissioner,* 123 F. (2d) 871 (C.C.A. 7), but the constitutional question was not discussed in either case.

In *Welch v. Henry,* 305 U. S. 134, relied upon by the Government, a Wisconsin statute enacted in 1935 was upheld as constitutional, although it was given retroactive effect to 1933. After referring to the cases upholding income tax statutes given retroactive effect for the year of the session in which the taxing statute is enacted, and in some instances during the year of the preceding session, the Supreme Court upheld the Wisconsin statute on the ground that the regular session of the Wisconsin Legislature which preceded the enactment of the statute was the 1933 session. The Court said:

> "And we think that the 'recent transactions' to which this Court has declared a tax law may be retroactively applied, Cooper v. United States, 280 U. S. 409, 411, 50 S. Ct. 164, 74 L. Ed. 516, must be taken to include the receipt of income *during the year of the legislative session preceding that of its enactment.* (Italics added.)
>
> * * * * * * *
>
> While the Supreme Court of Wisconsin, 223 Wis. 319, 271 N. W. 68, 72, thought that the present tax might 'approach or reach the limit of permissible retroactivity', we cannot say that it exceeds it."

The Government also refers (Br. p. 20) to the decision of the Tax Court of the United States in *Estate of John H. Wheeler v. Commissioner,* 1 T. C. 640, now pending before this Court. This case holds that the retroactive application of section 501 of the Second Revenue Act of 1940 to transactions occurring in 1938 is not unconstitutional. That case is distinguishable from the instant case not only because of the shorter period of retroactivity—two years as compared with four years—but also because the Tax Court felt that the particular facts justified the retroactive application of the statute. Thus the Tax Court said, pages 651-652:

> "It cannot be said that the application of the provisions of section 501(a) to section 112(b)(7) results in a harsh tax, since the gain recognizable thereunder is substantially less than the amount of gain which would have been taxable under section 115(c) * * *. The petitioners elected to be taxed under section 112(b)(7) and they cannot complain if such election resulted in a greater tax than they expected to pay * * *. As pointed out above, applying section 501(a) to section 112(b)(7), the gain recognizable was less than it would have been under section 115(c), so that the petitioners were benefited to that extent at least."

CONCLUSION.

The simple facts of this case are that Honolulu incorporated three subsidiaries to carry on operations in other states, that these subsidiaries operated at a loss and were liquidated, at which time Honolulu itself

realized the loss resulting from these ventures. The Government insists that this loss actually realized by Honolulu does not reduce earnings available for dividends, although it admits that if there had been a profit the earnings of Honolulu would have been increased by a transfer of the earnings of its subsidiaries. The Government apparently concedes that this result is highly illogical. It is also inequitable. Unless the statute compels such a result, logic and equity require a decision for the appellant. The statute does not require such a result if it is held that the operating deficits of the subsidiaries were absorbed by Honolulu. It is only by so holding that section 501 of the Second Revenue Act of 1940 operates equitably and its retroactive application to all prior Revenue Acts can be justified, as intended by Congress, "as but another aspect of the principle" of the *Sansome* case.

Dated, San Francisco,
April 6, 1944.

Respectfully submitted,
LEON DE FREMERY,
MORRISON, HOHFELD, FOERSTER,
SHUMAN & CLARK,
Attorneys for Appellant.

(Appendix Follows.)

Appendix.

Appendix

REVENUE ACT OF 1936.

SEC. 115. DISTRIBUTIONS BY CORPORATIONS. (49 Stat. 1682.)

(c) Distribution in Liquidation.—Amounts distributed in complete liquidation of a corporation shall be treated as a full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as a part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. Despite the provisions of section 117(a), 100 per centum of the gain so recognized shall be taken into account in computing net income, except in the case of amounts distributed in complete liquidation of a corporation. For the purpose of the preceding sentence, "complete liquidation" includes any one of a series of distributions made by a corporation in complete cancellation or redemption of all of its stock in accordance with a bona fide plan of liquidation and under which the transfer of the property under the liquidation is to be completed within a time specified in the plan, not exceeding two years from the close of the taxable year during which is made the first of the series of distributions under the plan. In the case of amounts distributed (whether before January 1, 1934, or on or after such date) in partial liquidation (other than a

distribution within the provisions of subsection (h) of this section of stock or securities in connection with a reorganization) the part of such distribution which is properly chargeable to capital account shall not be considered a distribution of earnings or profits.

No. 10665

United States
Circuit Court of Appeals
For the Ninth Circuit.

A. T. MARTIN and ALICE M. MARTIN,
Appellants,

vs.

CHARLOTTE L. SHEELY, JOHN H. SHEELY, JOE A. SHEELY and ROSS L. SHEELY, Copartners,
Appellees.

Transcript of Record

Upon Appeal from the District Court For the Territory of Alaska, Third Division

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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*Page numbering appearing at foot of page of original certified Transcript of Record.

In the District Court for the Territory of Alaska,
Third Division

No. A-2827

CHARLOTTE L. SHEELY, JOHN H. SHEELY, JOE A. SHEELY, and ROSS L. SHEELY,
Plaintiffs,

vs.

A. T. MARTIN and ALICE M. MARTIN,
Defendants.

COMPLAINT

Come now the plaintiffs above-named and for a first cause of action against defendants allege as follows:

I.

That during the month of June, 1941, the plaintiffs and defendants entered into oral negotiations for the purchase by the plaintiffs from the defendants, and the sale by the defendants to the plaintiffs, of the personal property comprising the whole of that certain dairy and milk distribution business conducted by the defendants under the trade name and style of "Step-And-Half-Ranch", and for the leasing of the land and premises used by the defendants for the conduct of the said business to the plaintiffs.

II.

That, as a result of the said oral negotiations, the plaintiffs, Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, with the defendants, entered into a "Conditional Sales Agreement", a "Lease", and a

"Grazing Permit", true and correct copies of which said instruments are hereto attached, marked Exhibits "A", "B", and "C", respectively, and by this reference made a part hereof the same as though set out herein in full, and that each of the said instruments was and is an integral part of the whole transaction, neither being acceptable to the plaintiffs without the others. [2]

III.

That by the terms of the said conditional sales agreement, the defendants agreed to sell to the plaintiffs, and the plaintiffs agreed to purchase of and from the defendants, the whole of that certain dairy and milk distribution business being then conducted by the defendants under the trade name and style of Step-And-Half Ranch, save and except the accounts receivable, but including the livestock, furniture and fixtures, farming implements and tools and motive equipment, all of which said property is set out in the inventory attached to the said conditional sales agreement, "Exhibit A", at and for the purchase price of Twenty-Eight Thousand Two Hundred Ninety-four Dollars ($28,294.00), payable $9800.00 upon the execution of the agreement, and $308.22 on the 10th day of August, 1941, and $308.22 on the 10th day of each month thereafter until the purchase price should be paid in full, with interest at the rate of 6% per annum from July 1st, 1941, until paid.

IV.

That the chief item contained in the inventory of property attached to the conditional sales agree-

ment, "Exhibit A", was fifty-six head of cows; that said cows were figured by the parties at Three Hundred Dollars ($300.00) per head, which accounted for $16,800.00 of the total purchase price of $28,294.00; that the defendants warranted that they were the lawful owners of the said cows and had the full right, power and authority to sell the same.

V.

That the plaintiffs, Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, on the 28th day of June, 1941, relying upon the representations of the defendants, entered into the said conditional sales agreement, "Exhibit A", executed the said lease "Exhibit B", and signed the said grazing permit, "Exhibit C", and paid to the defendants the sum of $9,800.00 on account of the purchase price of the property described in the said conditional sales agreement, $200.00 on account of the said lease, and $110.00 on account of the said grazing permit, and thereafter on or about July 1st, 1941, [3] entered into possession of the property and premises described in the said instruments.

VI.

That on the 28th day of June, 1941, at the insistance of the defendants, the plaintiff, Ross L. Sheely, did in writing guarantee the performance by the plaintiffs, Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, of the said conditional sales agreement and lease, a true and correct copy of which said guaranty is hereto attached, marked

"Exhibit D", and by this reference made a part hereof the same as though set out herein in full.

VII.

That the plaintiffs have performed to date the terms and conditions of the said conditional sales agreement, lease, grazing permit, and guaranty, and, in addition to the payments alleged in Paragraph V, above, have paid to the defendants upon the said Conditional Sales agreement "Exhibit A", the sum of $1541.10 and $450.00 interest, and upon the said lease, "Exhibit B", the sum of $1000.00, and have paid to the defendants the sum of $550.00 for their equity in a truck being purchased by the defendants from Wells Motor Company, Inc., of Anchorage, Alaska, and have paid to defendants the sum of $2000.00 for hay and grain which the defendants had on order at the time of the execution of the conditional sales agreement, and as in said conditional sales agreement provided, and have purchased additional equipment for the dairy and made improvements upon the premises at a cost of $2513.00.

VIII.

That at the time of the execution of the said Conditional Sales Agreement, lease, grazing permit, and guaranty, and for a long time prior thereto, a large number of the cows sold to the plaintiffs and described in the said conditional sales contract were diseased and infected with Bang's Disease or contagious abortion, which fact was well known to the defendants; and unknown to the plaintiffs; but,

notwithstanding such knowledge upon the part of the defendants, and with the intent to injure the plaintiffs, the defendants [4] sold and delivered the said cows to the plaintiffs and accepted from the plaintiffs a portion of the purchase price thereof as hereinabove alleged.

IX.

That since the 28th day of June, 1941, the date of the execution of the instruments hereinabove described, the plaintiffs have of necessity and because of the said disease, killed and disposed of eight of the cows purchased from the defendants and have received therefor the total sum of $832.45, which amount the plaintiffs allege is approximately one-third of the value of clean, uninfected dairy cows.

X.

That all of the said cows were purchased by the plaintiffs as and for a dairy herd, which fact was well known to the defendants, and the said disease with which the said herd was and is infected renders the herd of little value for dairy purposes.

XI.

That the plaintiffs have suffered damages by reason of the wrongful acts and omissions of the defendants herein alleged, and will suffer irreparable damage if they are required to perform their agreements with the defendants, as herein described, and as hereto attached and marked "Exhibits A, B, C, and D."

XII.

That the plaintiffs have no plain, speedy, and adequate remedy at law.

And For a Second Cause of Action Against the Defendants, Plaintiffs Allege:

I.

That on the 28th day of June, 1941, and for a long time prior thereto, the plaintiffs owned a large dairy herd, and operated a dairy business near the town of Palmer, in the Third Judicial Division of the Territory of Alaska, and that the cows comprising the said dairy herd were free from the disease known as Bang's Disease, or contagious abortion. [5]

II.

That on the said date, and for a long time prior thereto, the defendants owned a large herd of cows, and operated a dairy business near the town of Anchorage, in the Third Judicial Division of the Territory of Alaska.

III.

That on the said date, and for a long time prior thereto, the dairy herd of the defendants was infected with the said disease known as Bang's Disease, or contagious abortion, which fact was well known to the defendants, and unknown to the plaintiffs.

IV.

That on the 28th day of June, 1941, in violation of law, the defendants, without disclosing to the plaintiffs the fact that the said herd was diseased,

sold to the plaintiffs fifty-six cows and one bull comprising the entire dairy herd of the defendants, and warranted that they had full right, power, and authority to sell the same.

VI.

That the plaintiffs, not knowing that the cows which they purchased from the defendants were infected with Bang's Disease, intermingled said cows with those of their own herd, and, as a result, thereof, their own dairy herd has become infected with the said disease, all to their damage in the sum of $10,000.00.

Wherefore, plaintiffs pray:

1. That the Conditional Sales Agreement, "Exhibit A", described in plaintiffs first cause of action be by this court decreed illegal and void;

2. That the lease, "Exhibit B", the Grazing Permit, "Exhibit C", and the Guaranty, "Exhibit D", be rescinded, cancelled, and declared void as being part of the same transaction and based upon and supported by the illegal agreement, "Exhibit A";

3. That the plaintiffs have judgment against the defendants, and each of them, for the sum of $16,163.10 on account of their first [6] cause of action;

4. That the plaintiffs have judgment against the defendants, and each of them, for the sum of $10,000.00 on account of their second cause of action;

5. That plaintiffs have such other and further

relief, as to the court may seem just and equitable in the premises;

6. That plaintiffs have judgment for their costs.

7. That the defendants be restrained and enjoined during the pendency of this cause from exercising any of the remedies provided for the defendants by the said conditional sales agreement, lease, grazing permit, and guaranty in the event of default by the plaintiffs.

W. N. CUDDY
Attorney for the plaintiffs [7]

United States of America
Territory of Alaska—ss.

Ross L. Sheely and Charlotte L. Sheely being first duly sworn on oath, depose and say:

That I am one of the plaintiffs named in the foregoing complaint which I have read and know the contents thereof, and that the statements and allegations therein contained are true as I verily believe.

ROSS L. SHEELY
CHARLOTTE L. SHEELY

Subscribed and sworn to before me this 27th day of December, 1941.

[Seal] W. N. CUDDY
Notary Public in and for Alaska. My commission expires: 8/29/45. [8]

EXHIBIT "A"

(Copy)

CONDITIONAL SALES AGREEMENT

This Agreement, made and entered into this 26th day of June, 1941, by and between A. T. Martin and Alice M. Martin, husband and wife, of Anchorage, Alaska, hereinafter called the "sellers", Charlotte L. Sheely, John H. Sheely and Joe A. Sheely, of the same place, hereinafter called the "buyers",

WITNESSETH:

For and in consideration of the mutual covenants and agreements hereinafter set forth, it is agreed as follows:

First: The sellers agree to sell, and the buyers agree to purchase the following described personal property for the price and upon the terms herein set forth, to-wit:

> The whole of that certain dairy and milk distribution business now being conducted by the sellers under the trade name and style of Step-and-Half Ranch, at and around Anchorage, Alaska, save and except the accounts receivable of the sellers, but including the livestock, furniture and fixtures, farming implements and tools and motive equipment that are set forth and particularly described in the hereto attached inventory marked Exhibit "A", which is by reference incorporated in and made a part of this description; and also including the good will of the sellers in and to said dairy and milk distribution business.

Exhibit "A"—(Continued)

for the sum of Twenty-Eight Thousand Two Hundred Ninety-Four Dollars ($28,294.00), payable as follows: Nine Thousand Eight Hundred Dollars ($9,800.00) in cash upon the execution of this agreement, the receipt of which is hereby acknowledged by the sellers, and the balance of Eighteen Thousand Four Hundred Ninety-Four Dollars ($18,494.00) in lawful money of the United States at the rate of Three Hundred Eight & 22/100 Dollars ($308.22) on the 10th day of August, 1941, and Three Hundred Eight & 22/100 Dollars ($308.22) on the 10th day of each and every month thereafter until [9] the whole of said balance shall have been paid. Interest on the unpaid balance shall be paid monthly, commencing August 10, 1941, at the rate of Six Percent (6%) per annum from the first day of July, 1941, until paid. Provided, however, that the buyers shall have the option of anticipating any or all of said monthly deferred payments at any time that they may choose to do so.

Second: The buyers hereby agree to pay the full sum above specified, together with interest, at the times and in the manner herein set forth, but it is mutually understood and agreed that the buyers shall have a grace period of ten (10) days from and after the 10th day of each month within which to make the monthly payment with interest then due. All of such payments shall be made by paying the same to the credit of the sellers at the First National Bank of Anchorage, Alaska, or at such other place

Exhibit "A"—(Continued)

in Anchorage, Alaska, as may be designated in writing by the sellers.

Third: It is specifically agreed that title to said personal property is to remain with and be in the sellers until the buyers have performed all of the terms and conditions herein set forth. It is further understood and agreed that the buyers shall have possession of the property covered by this agreement on the 1st day of July, 1941, and shall continue in the possession thereof unless and until they shall default in any of the terms, conditions and covenants herein contained.

Fourth: It is agreed that provided the cows, the bull, the caterpillar tractor, ensilage cutter, manure spreader, mower and windrower and the 10-horse motor are properly marked for identification, they may be moved from the Anchorage Precinct to lands being farmed by the buyers in the Palmer Recording Precinct, but not otherwise. The buyers further specifically agree that they will not remove any of the other personal property from the lands being operated by them either under lease from the sellers or in connection with their milk dairy distribution business in the Anchorage Precinct, Territory of Alaska, without the written consent of the sellers. They further agree not to permit any other person or persons to have possession of any of the property sold hereby, without the written consent of the sellers. [10]

Fifth: The buyers further agree to be fully responsible and to remain bound for the full pur-

Exhibit "A"—(Continued)

chase price of the property covered by this agreement should the same become lost, damaged or destroyed by fire or otherwise.

Sixth: It is understood and expressly agreed that the buyers have inspected the property covered by this agreement and are familiar with the condition thereof and that the same is sold to the buyers without any warranties or representations of any kind or character whatsoever on the part of the sellers, save and except that the sellers warrant and agree that they are the lawful owners thereof and have full right, power and authority to sell and dispose of the same and that there are no existing liens or encumbrances against said property or any part or portion thereof.

Seventh: The sellers agree that the buyers may dispose of the increase from the dairy herd in such manner as they see fit, except that it is agreed that the herd shall be maintained in not less than the present numbers, during the life of this contract, and any replacements to the dairy herd shall be bound by all of the terms and conditions hereof. The buyers agree that they will keep and maintain the other personal property covered by this agreement in good repair during the life hereof.

Eighth: The buyers agree that during the life of this agreement they will pay all taxes, assessments or charges that may be levied or laid against or upon said property, when the same shall become due; and that they will not permit any mechanics' material men's or other liens of any kind or nature to become effective against the same.

Exhibit "A"—(Continued)

Ninth: It is understood that the sellers have on order grain and hay of an approximate landed cost of Two Thousand Dollars ($2,000.00) and the buyers agree to pay to the sellers, on or before the 1st day of September, 1941, the cost landed price at [11] Anchorage, Alaska, for said grain and hay, over and above and in addition to the payments hereinbefore agreed to be made by the buyers; and the buyers further agree that they will take over and assume from the sellers the purchase contract for a truck of the approximate value of One Thousand Seven Hundred Dollars ($1,700.00) being purchased from the Wells Motor Company of Anchorage, Alaska, and to pay to the sellers on or before the 1st day of September, 1941, the equity of the sellers in the purchase contract for said truck in the sum of Five Hundred Fifty Dollars ($550.00); it being further understood and agreed that the present truck being used in the milk distribution business is to be turned in to the Wells Motor Company upon the arrival of the new truck, and the buyers may have the right to use the same until the arrival of said new truck, entirely at their own risk.

Tenth: The sellers agree to make available for the inspection of the buyers their records and accounts of the business conducted by them under the name and style of Step-And-Half Ranch.

Eleventh: The sellers further agree that they will not engage in the dairy or milk distribution

Exhibit "A"—(Continued)

business in the Anchorage Precinct, Territory of Alaska, for a period of ten (10) years from and after the 1st day of July, 1941, provided that the buyers do not default in the terms and conditions of this agreement or under the lease of the real estate from the buyers executed contemporaneously herewith.

Twelfth: It is understood and agreed that the buyers shall not assign this agreement without the written consent of the sellers first had and received and that they shall not mortgage, hypothecate or otherwise charge or encumber their rights or equities hereunder, and shall not permit said property to be attached, seized or levied upon under any process of any court of law.

Thirteenth: It is agreed that time shall be of the essence of this agreement and that, should the buyers default in any of the [12] payments, terms, conditions and covenants hereof, then and in any of such events the sellers may at their option immediately declare the entire balance due hereunder to be forthwith due and payable and may immediately retake possession of said property with or without process of law, and all payments theretofore made shall be retained by the sellers as rent and liquidated damages; but in no event shall the buyers be released from any of their obligations under this contract to pay the full purchase price for said property unless specifically so released by the sellers in writing or by operation of law in accordance with the provisions of the Conditional

Exhibit "A"—(Continued)

Sales Act as now in force and effect in the Territory of Alaska. It is further agreed that a waiver by the sellers of any of the terms or provisions hereof shall not be construed to be a waiver as to any subsequent violation or violations that may occur, nor shall it be construed to be a waiver with respect to payments being required on the due dates as herein set forth.

Fourteenth: Each and every clause, term, covenant, provision and condition of this agreement shall inure to the benefit of, descend to and become binding upon the heirs, executors, administrators and assigns of the respective parties hereto, subject to the restrictions as to assignment or alienation by the buyers as hereinabove set forth.

In Witness Whereof, the parties hereto have hereunto executed this agreement on the day and year first hereinabove written.

[Seal] A. T. MARTIN
[Seal] ALICE M. MARTIN
Sellers
[Seal] CHARLOTTE L. SHEELY
[Seal] JOHN H. SHEELY
[Seal] JOE A. SHEELY
Buyers

Witnesses:
THOMAS M. DONOHOE
W. N. CUDDY [13]

Exhibit "A"—(Continued)

(Copy)

United States of America
Territory of Alaska—ss.

This Is To Certify, that on this 28th day of June, 1941, before me, the undersigned, a notary public in and for the Territory of Alaska, duly commissioned and sworn, personally appeared A. T. Martin, Alice M. Martin, Charlotte L. Sheely, John H. Sheely and Joe A. Sheely, each to me personally known and to me known to be the individuals described in and who executed the foregoing instrument of writing, and each acknowledged to me that he/she signed and sealed the same freely and voluntarily for the uses and purposes therein mentioned.

In Witness Whereof, I have hereunto set my hand and affixed my official seal on the day and year in this certificate first above written.

[Seal] THOMAS M. DONOHOE
Notary Public for Alaska. My commission expires Aug. 16, 1944. [14]

Exhibit A

56—Cows
1—Bull
1—Caterpillar
1—Ensilage Cutter
1—Breaking Plow
1—Three-bottom Plow
1—Grain Drill
1—Manure Spreader

Exhibit "A"—(Continued)

1—Disc Harrow
1—Spike
1—Spring Tooth Harrow
1—Hay Rake
1—Mower and Windrower
1—Motor 10-horse
1—Motor with Emery
1—Chain Hoist 1½ T.
Milking Machines 3 U
1—Electric Heater
1—Dairy Scale
48—Salt Cups
25—Drinking Cups
1—Cow Sling
1—Wagon
1—Sled
1—Milk Cart
1—Boiler
1—Pasteurizer
1—Cooler
Cooler Covers
1—Separator
Bottle and capper
1—Tank
Motor Pump and Pipe
1—Thermometer
1—Bottle Washer
1—Churn
1—Compressor for Milk M.
1—Pump
1—Pump

Exhibit "A"—(Continued)

1—Pump
Dollies Milk
18—Milk Cans 10-gal.
4—Milk Cans 5-gal.
10— " " 3-gal.
10— " " 2-gal.
10— " " 1-gal.
41—Bottle Crates qts.
12— " " pts.
100— " " ½ pts.
8—Bottles qts.
" pts.
" ½ pts. [15]
3—Beds and Mattresses
2—Wardrobes
1—Dresser
4—Chests of Drawers
1—Sewing Machine
1—Dining Table
8—Chairs
1—Cook Stove
1—Electric Heater
1—Cabinet
1—Filing Cabinet
1—Desk
1—Filing Cabinet
1—Typewriter
1— " Table
1—Adding Machine
1—Check Machine
1—End Table

Exhibit "A"—(Continued)

1—Davenport
2—Chairs
1—Chair
1—Table
1—Radio and Attachment
1—Radio Table
Cooking Utensils
Dishes and Silver
Bunk House
2—Double Deck Beds
2—Cots and Mattresses
1—Heater
2—Chairs
3—Chairs
5—Blankets—wool
12— " —cotton
Seed and Fertilizer
Planting and Manure
1—bbl. Wyandotte C.C.
3—Drums Lime
8—Cartons Discs
2—8-place Carriers
3—6 " "
500—Paper Bottles qts.
200— " " pts.
300— " " ½ pts.
40—c/s qt. bottles
10— " pt. "
35— " ½-pt. " [16]

EXHIBIT B

(Copy)

LEASE

This Indenture, made and entered into this 26th day of June, 1941, by and between A. T. Martin and Alice M. Martin, husband and wife, of Anchorage, Alaska, hereinafter called the "lessors", Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, of the same place, hereinafter called the "lessees",

WITNESSETH:

For and in consideration of the mutual covenants and agreements hereinafter set forth it is agreed as follows:

The lessors do hereby lease, let and demise unto the lessees, the following described premises and property, to-wit:

> The North Three Hundred Sixty (360) feet of Tract Number Twenty-seven (27) and of Tract Number Twenty-eight (28) of United States Survey Number 1456, Fourth Addition to Anchorage Townsite in T. 13 N., R. 3 W., Seward Meridian, Anchorage Precinct, Territory of Alaska, according to the official map and plat thereof now of record in the office of the United States Commissioner and ex-officio recorder for the Anchorage Precinct; with the appurtenances,

for a term of ten (10) years commencing with the 1st day of July, 1941, and ending with the 30th day

of June, 1951, at the monthly rental of the sum of Two Hundred Dollars ($200.00) per month.

All rentals shall be payable in lawful money of the United States of America in advance on the first day of each and every month during said term, by depositing the same to the creditor of the lessors at the First National Bank, Anchorage, Alaska, or to such other agent of the lessors at Anchorage, Alaska, that they may designate in writing. The lessors hereby acknowledge the receipt of the sum of Two Hundred Dollars ($200.00) in payment of the rental for the month of July, 1941.

The lessees and each of them hereby covenant and agree to pay the entire rent for the full term of this lease to the [17] lessors at the times and in the manner herein specified. It is agreed that default in the payment of rentals for a period of ten (10) days after the same shall become due, shall work a forfeiture of this lease at the option of the lessors.

It is expressly understood and agreed that the leased premises shall be used for dairy purposes and for no other purpose without the written consent of the lessors first had and received.

The lessees hereby covenant and agree not to use the premises herein leased or to permit them to be used for any purpose that will increase the rate of fire insurance on the buildings situated thereon, over the rate ordinarily charged; and that they will not install or permit to be installed any apparatus that will cause a higher rate of fire insurance than is now charged and will not keep or per-

mit to be kept or maintained any apparatus or thing prohibited by the rules or regulations of the regular fire insurance companies. The lessees further agree that in the occupancy and use of the said leased premises they will comply with all of the laws of the Territory of Alaska and of the United States of America, and will not use or permit said premises to be used for any unlawful purpose or purposes.

The lessees are hereby granted permission to erect upon the leased premises any buildings or structures that they may desire for use in conducting a dairy or dairy business, and it is agreed that they may remove the same at the expiration of this lease or prior thereto if they are not in default in any of the terms and conditions herein set forth. Provided, however, that before removing the same they shall give notice thereof to the lessors in writing for a period of at least fifteen (15) days, and the lessors shall have the option within said fifteen (15) day period, of purchasing said buildings or structures at the cost price to the lessees. It is further agreed that if they should [18] remove any such buildings or structures, they shall restore the land to its original condition. The lessees further covenant and agree that during the term of this lease they will maintain the buildings and structures now situated upon the leased premises in as good a condition as they now are, reasonable wear and tear and damage by fire excepted.

The lessees agree not to permit any material men's, mechanics' or other liens of any kind or

nature, or charges or assessments to become effective against said leased premises or property during the term of this lease; and they further agree that the lessors may post notices of non-liability against any material men's or laborers' liens and that the lessees will keep and maintain said notices posted during the life hereof.

It is understood and agreed that this lease is made subject to an easement which has been granted by the lessors to the City of Anchorage, Alaska, for a water pipe through the land covered hereby.

It is understood and agreed that the lessees shall not assign this lease or sub-let or under-let the whole or any part or portion of the premises covered hereby, without first obtaining the written consent of the lessors.

The lessors do hereby covenant that upon the payment of the rentals and the performance of all of the agreements and conditions hereof by said lessees to be paid and performed as herein set forth, said lessees shall peaceably and quietly hold and enjoy the above described premises during the full term herein specified.

It is further covenanted and agreed that if default be made in the payment of the rentals as above specified or in the keeping of any of the agreements herein agreed to be kept by the lessees, then it shall be lawful for the said lessors at their [19] option to terminate this lease; to re-enter upon said premises and property and to remove all per-

sons therefrom; but the excercise of such option shall not be construed to release the lessees from any covenants and agreements herein contained, including damages for the non-payment of rentals as herein specified. The lessees further agree that at the expiration of the term of this lease either by lapse of time or by forfeiture as above specified, they will quit and surrender said premises quietly and peaceably to the lessors.

It is understood that should the lessors fail to excercise their option to terminate this lease because of the failure to pay rent when due or because of the failure to comply with some or one of the other covenants herein contained, this shall not be construed to be a waiver of the right of the lessors to terminate the same at their option for any future default or defaults that may occur.

Time shall be of the essence of this lease; and it is also agreed that the same shall inure to the benefit of, descend to and become binding upon the heirs, executors, administrators and assigns of the respective parties hereto, and the lessees do hereby bind themselves jointly and severally that they will keep and perform all of the covenants and conditions hereof, including the payment of the rentals herein specified.

In Witness Whereof, the parties hereto have caused this indenture to be duly executed on the day and year first hereinabove written.

[Seal] A. T. MARTIN
[Seal] ALICE M. MARTIN
Lessors
[Seal] CHARLOTTE L. SHEELY
[Seal] JOHN H. SHEELY
[Seal] JOE A. SHEELY
Lessees

Witnesses:
THOMAS M. DONOHOE
W. N. CUDDY [20]

United States of America
Territory of Alaska—ss.

This Is To Certify, that on this 28th day of June, 1941, before me, the undersigned, a notary public in and for the Territory of Alaska, duly commissioned and sworn, personally appeared A. T. Martin, Alice M. Martin, Charlotte L. Sheely, John H. Sheely and Joe A. Sheely, each to me personally known and to me known to be the individuals described in and who executed the foregoing instrument of writing, and each acknowledged to me that he/she signed and sealed the same freely and voluntarily for the uses and purposes therein mentioned.

In Witness Whereof, I have hereunto set my hand and affixed my official seal on the day and year first above written.

[Seal] THOMAS M. DONOHOE
Notary Public for Alaska. My commission expires August 16, 1944. [21]

EXHIBIT "C"

(Copy)

GRAZING PERMIT

Whereas, Asa T. Martin holds a lease on school lands from the Territory of Alaska covering Lots 2, 3, and 4, Sec. 16, Twp. 13 N., R. 3 W., Seward Meredian, Anchorage Precinct, and also the SW¼ of the NW½, SE¼ of the NW¼, and the SW¼ of the NE¼ of Sec. 16, 13 N., 3 W., Seward Meridian dated March 20th, 1935; and has applied to the Governor of the Territory for a new lease to last for a period of ten years; and

Whereas, the said Asa T. Martin is this day selling to Charlotte L. Sheely, John N. Sheely and Joe A. Sheely his milk and dairy distribution business of Anchorage, Alaska, and is leasing to said persons a tract of land for a period of ten years commencing with July 1, 1941, adjacent to the school lands above mentioned.

Now, Therefore, in consideration of the premises it is agreed by the said Asa T. Martin that the said Charlotte L. Sheely, John H. Sheely and Joe A. Sheely may use the said school lands leased by him as aforesaid for dairy purposes for such period of time as the lease mentioned above is not in default, and subject to the conditions as to use set forth in the lease from the Territory to the said Asa T. Martin.

The said Charlotte L. Sheely, John H. Sheely and Joe A. Sheely agree to pay to the said Asa T.

Martin the sum of $110.00 per year payable on the due dates specified in the said Territorial lease.

Dated at Anchorage, Alaska, this 28th day of June, 1941.

A. T. MARTIN
CHARLOTTE L. SHEELY
JOHN H. SHEELY
JOE A. SHEELY

Witnesses:

THOMAS M. DONOHOE
W. N. CUDDY [22]

EXHIBIT "D"

(Copy)

GUARANTY OF PERFORMANCE OF CONTRACT

This Guaranty made this 28th day of June, 1941, by the undersigned Ross L. Sheely, of Anchorage, Alaska, Witnesseth:

Whereas, Charlotte L. Sheely, John H. Sheely and Joe A. Sheely have entered into a certain Conditional Sales Agreement bearing date the 26th day of June, 1941 with A. T. Martin and Alice M. Martin for the purchase of that certain dairy and milk distribution business known as Step-and-Half Ranch for the sum of $28,294.00; and

Whereas, the said Charlotte L. Sheely, John H. Sheely and Joe A. Sheely are the lessees named in that certain lease bearing date the 26th day of June, 1941, wherein A. T. Martin and Alice M. Martin are named as the lessors;

Now, Therefore, for and in consideration of the sum of One Dollar ($1.00) to me in hand paid by the said A. T. Martin and Alice M. Martin, the receipt whereof is hereby acknowledged, I do hereby guarantee, promise, and agree to and with them, that the above-named Charlotte L. Sheely, John H. Sheely and Joe A. Sheely will well and faithfully perform and fulfill everything by the hereinabove described Conditional Sales Agreement and Lease on their part and behalf to be performed and fulfilled, at the times and in the manner provided therein. And I do hereby expressly waive and dispense with any demand upon the said Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, and any notice of any nonperformance on their part.

In Witness Whereof, I have hereunto set my hand and seal this 28th day of June, 1941.

[Seal] ROSS L. SHEELY

In the presence of:

THOMAS M. DONOHOE

W. N. CUDDY

Service accepted this 13th day of May, 1942.

.....

Attorney for A. T. Martin and Alice M. Martin.

[Endorsed]: Filed May 13, 1942. [23]

[Title of District Court and Cause.]

DEMURRER

Come now the defendants above-named and demur to the complaint of the plaintiffs in the above-entitled action upon the following grounds, to-wit:

1. That the first cause of action thereof does not state facts sufficient to constitute a cause of action.

2. That the second cause of action thereof does not state facts sufficient to constitute a cause of action.

3. That several cause of action have been improperly united.

THOMAS M. DONOHOE,
Attorney for Defendants.

Service of the Foregoing Demurrer By Receipt of Copy Thereof Acknowledged on This

W. N. CUDDY,
Attorney for the Pltfs.

[Endorsed]: Filed May 21, 1942. [24]

[Title of District Court and Cause.]

MINUTE ORDER OVERRULING DEMURRER

Now at this time, the above-entitled cause having heretofore come on for hearing on defendants' Demurrer to plaintiffs' Complaint on the 12th day of June, 1942, the Court having granted counsel ten days to submit briefs, and the Court being fully and duly advised in the premises,

It Is Ordered that defendants' Demurrer be, and the same hereby is, overruled, and an exception granted defendants. [25]

[Title of District Court and Cause.]

ANSWER

Come now the defendants above-named and for answer to the complaint of the above-named plaintiffs admit, deny and allege as follows, to-wit:

I, II, III.

Referring to paragraphs I, II and III to plaintiffs' complaint, defendants admit the same.

IV.

Referring to paragraph IV of plaintiffs' complaint defendants admit the same except that defendants deny that there was any segregation of value for the cows or any other item embodied in said conditional sales contract, "Exhibit A".

V.

Referring to paragraph V of plaintiffs' complaint defendants admit the same except that defendants deny that said plaintiffs relied upon the representations of the defendants.

VI.

Referring to paragraph VI of plaintiffs' complaint defendants admit that plaintiff Ross L. Sheely guaranteed the performance of the other

plaintiffs; deny that he did this at the insistence of the defendants; and allege that this method of handling the transfer of the business from defendants to plaintiffs was proposed by the said Ross L. Sheely because he did not wish to appear directly as a purchaser in view of prior commitments to the Matanuska Valley Farmers Cooperating Association. [26]

VII.

Referring to paragraph VII of plaintiffs' complaint defendants specifically deny that the plaintiffs have performed to the date of said complaint the terms and conditions of the said conditional sales agreement, lease, grazing permit, and guaranty; deny that plaintiffs have purchased additional equipment for the dairy and made improvements upon the premises at a cost of $2513.00 or any other sum; admit that plaintiffs made the payments in said paragraph specified; and specifically allege the said plaintiffs did not make any of the payments specifically required to be made by the terms of said conditional sales contract, lease and guarantee subsequent to the month of December, 1941, and were and are in default by reason of such nonpayments.

VIII.

Referring to paragraph VIII of plaintiffs' complaint defendants deny the same and each and every allegation therein contained.

IX.

Referring to paragraph IX of plaintiffs' complaint defendants admit that plaintiffs have killed

and disposed of the cows therein mentioned but defendants deny that the same were killed or disposed of by necessity and because of said disease.

X.

Referring to paragraph X of plaintiffs' complaint defendants admit that said cows were purchased for a dairy herd and defendants deny each and every other allegation in said paragraph contained.

XI and XII.

Referring to paragraphs XI and XII of plaintiffs' complaint defendants deny the same and each and every allegation in said paragraphs contained.

[27]

And for Answer to Plaintiffs' Second Cause of Action Defendants Admit, Deny and Allege as Follows:

I.

Referring to paragraph I of plaintiffs' second cause of action defendants admit that plaintiffs owned a dairy herd near Palmer, Alaska, and defendants deny each and every other allegation in said paragraph contained.

II.

Referring to paragraph II of plaintiffs' second cause of action defendants admit the same.

III.

Referring to paragraph III of plaintiffs' second cause of action defendants deny the same and each and every allegation therein contained.

IV.

Referring to paragraph IV of plaintiffs' second cause of action defendants admit that they sold to plaintiffs fifty-six cows and one bull on the 28th day of June, 1941, and warranted that they had right to sell the same; and defendants deny each and every other allegation in said paragraph contained.

V.

Referring to paragraph V (marked VI) of plaintiffs' second cause of action defendants deny the same and each and every allegation therein contained.

And By Way of First Counter-Claim and First Cross-Complaint Defendants Allege as Follows:

I.

That on the 28th day of June, 1941, the defendants at the special instance and request of the plaintiffs sold to the plaintiffs in accordance with the terms and conditions of a certain written conditional sales agreement, a true copy of which is hereto attached, Marked Exhibit 1, and by reference incorporated in and [28] made a part hereof, that certain dairy and milk distribution business then being conducted at and about Anchorage, Alaska, under the trade name and style of Step-and-Half Ranch, and including certain personal property as in said conditional sale contract described, for the sum of $28,294.00; $9,800.00 down, $308.22 on the 10th day of August, 1941, and $308.22 on the 10th day of each month thereafter until the whole of

the balance shall have been paid with interest on the balance at a rate of 6% per annum from July 1st, 1941, payable monthly.

II.

That on said 28th day of June, 1941, for a valuable consideration, plaintiff Ross L. Sheely did in writing guarantee the payments as above specified and did guarantee the performance of the terms and conditions of said conditional sales contract by the remaining plaintiffs in this action. That hereto attached, marked exhibit 4, and by reference incorporated in and made a part hereof, is a full, true and correct copy of said guarantee.

III.

That said conditional sales agreement by its terms provides that the plaintiffs shall have a grace period of ten days within which to make the monthly payment with interest then due but that other than that time shall be of the essence of said agreement and that should the buyers default in any of the payments, terms, conditions and covenants of said agreement then the sellers, defendants herein, may at their option declare the entire balance forthwith due and payable. That said agreement by its terms further provides that plaintiffs, buyers therein, shall not permit any other person or persons to have possession of any of the property covered by the same without the written consent of the sellers, defendants herein.

IV.

That the plaintiffs have defaulted in the terms and [29] conditions of said conditional sales contract in the following particulars, to-wit:

(1) That said plaintiffs have failed, neglected and refused to make the monthly payment of $308.22, together with interest on the balance due under said contract, due on the 10th day of January, 1942, within the time limited by said conditional sales contract or at all; and that said plaintiffs have failed, neglected and refused to make the monthly payments of principal and interest due each month since January, 1942, within the time allowed by said contract or at all.

(2) That contrary to the terms and provisions of said conditional sales contract the plaintiffs have permitted other persons to have the possession and control of personal property covered thereby without first obtaining the written consent of the defendants, specifically, the caterpillar tractor covered thereby.

(3) That contrary to the terms and provisions of said conditional sales contract the plaintiffs have not maintained the dairy herd in number equivalent to that at the time of said sale.

V.

That in accordance with the terms of said conditional sales contract the defendants have elected, and do hereby elect, because of the default of the plaintiffs in making the payments as in said contract provided for and in otherwise defaulting in

the performance of the terms, conditions and covenants of said contract to declare the entire unpaid balance of principal and interest due under said contract immediately due and payable. That said plaintiffs paid to defendants the sum of $1541.10, and no more, upon the unpaid balance of principal of $18,494.00 as in said contract provided; together with interest at 6% per annum from July 1, 1941, to December 10th, 1941, on said unpaid balance; and that by reason thereof there is now due, owing and unpaid to [30] defendants from plaintiffs the sum of $16,952.90, together with interest at the rate of 6% per annum from December 10th, 1941, and although defendants have made demand upon plaintiffs for the payment thereof plaintiffs have wholly failed, neglected and refused to pay the same or any part or portion thereof.

And for a Second Counter-Claim and Second Cross-Complaint Defendants Allege as Follows:

I.

That on the 28th day of June, 1941, the defendants at the special instance and request of the plaintiffs leased and let to said plaintiffs certain real property situated in the Anchorage Precinct, Territory of Alaska, for a term of ten years commencing with July 1st, 1941, and ending June 30th, 1951, at the monthly rental of $200.00 per month, payable monthly in advance on the first day of each and every month during said term. That hereto attached and marked Exhibit 2 is a full, true, and

correct copy of said lease, and the same is by reference incorporated in and made a part hereof.

II.

That on said 28th day of June, 1941, for a valuable consideration, plaintiff Ross L. Sheely did in writing guarantee the payment of rentals as above specified and did guarantee the performance of the terms and conditions of said lease by the remaining plaintiffs in this action. That hereto attached, marked Exhibit 4, and by reference incorporated in and made a part hereof is a full, true and correct copy of said guarantee.

III.

That the plaintiffs have paid to defendants the rentals for the months of July, August, September, October, November and December, 1941, and no more, and plaintiffs have wholly failed, neglected and refused to pay to defendants the rentals for the months January to October, both inclusive, 1942, and by reason thereof there is now due, owing and unpaid to [31] defendants from plaintiffs the sum of $2,000.00, together with interest at 6% per annum on each monthly payment of $200.00 thereof.

IV.

That under the terms and conditions of said lease the defendants are entitled to the immediate possession of said leased premises because of the default in the payment of the rentals as therein specified and as above set forth, and so elect to obtain the same.

And for a Third Counter-Claim and Third Cross-Complaint Defendants Allege as Follows:

I.

That on the 28th day of June, 1941, the defendants at the special instance and request of the plaintiffs, granted to said plaintiffs a grazing permit for certain lands then and now leased by defendants from the Territory of Alaska and situated in Anchorage Precinct, Territory of Alaska, upon the payment to the defendants of an annual rental of $110.00. That hereto attached, marked Exhibit 3, and by reference incorporated in and made a part hereof is a full, true and correct copy of said grazing permit.

II.

That by the terms of said grazing permit said annual rental was due to defendants at the date of the lease between defendants and said Territory of Alaska, to-wit: August 19th. The said plaintiffs have wholly failed, neglected and refused to pay to defendants said sum of $110.00 so due to them on the 19th day of August, 1942, or any part or portion thereof, and by reason thereof said plaintiffs are in default. That said grazing permit further provides that the same shall terminate in the event of a default by the plaintiffs in the performance of that certain lease dated June 28th, 1941, a true copy of which is hereto attached, marked Exhibit 2, and by reference incorporated [32] in and made a part hereof. That the plaintiffs have defaulted in the terms of said lease as hereinabove set forth in defendants' Second Coun-

ter-Claim and Second Cross-Complaint to which reference is hereby made for all of the particulars therein contained.

III.

That by reason thereof the defendants are entitled to the immediate possession of the premises described in said grazing permit and the cancellation thereof.

Wherefore defendants having fully answered plaintiff's complaint pray that plaintiffs take nothing by reason thereof and that the same be dismissed and that defendants have judgment against said plaintiffs and each of them as follows:

1. On defendants' first counter-claim and first cross-complaint for the sum of $16,952.90, together with interest at the rate of 6% per annum from December 10th, 1941;

2. On defendants' second counter-claim and second cross-complaint for the sum of $2,000.00, together with interest at 6% per annum on each monthly payment of $200.00 thereof commencing with January 1st, 1942; that defendants have immediate possession of the premises and property mentioned and described in the lease set forth in said counter-claim and cross-complaint;

3. On defendants' third counter-claim and third cross-complaint that defendants have immediate possession of the premises and property mentioned and described in the grazing permit set forth in said counter-claim and cross-complaint and that the same be cancelled.

4. For defendants' costs and disbursements in this action incurred.

JOHN E. MANDERS,
THOMAS M. DONOHOE,
Attorneys for Defendants.

[33]

United States of America
Territory of Alaska—ss.

Asa T. Martin, being first duly sworn, upon his oath says:

I am one of the defendants named in the foregoing answer and cross-complaint and make this affidavit of verification for and on behalf of said defendants; that I have read the same, know the contents thereof, and that the same is true as I verily believe.

ASA T. MARTIN.

Subscribed and sworn to before me this 2d day of November, 1942.

[Seal] THOMAS M. DONOHOE,
Notary Public for Alaska. My commission expires Aug. 16, 1944.

Service of the Foregoing Answer by Receipt of Copy Thereof Acknowledged on This 2d day of Nov. 1942.

W. N. CUDDY,
Attorney for the Pltfs. [34]

EXHIBIT "1"

[Printer's Note: Exhibit "1" is not reproduced here, as it is the same as Exhibit "A" attached to the Complaint, and printed in full, starting at page 10 of this printed record.]

EXHIBIT "2"

[Printer's Note: Exhibit "2" is not reproduced here, as it is the same as Exhibit "B" attached to the Complaint, and printed in full, starting at page 21 of this printed record.]

EXHIBIT "3"

[Printer's Note: Exhibit "3" is not reproduced here, as it is the same as Exhibit "C" attached to the Complaint, and printed in full, starting at page 27 of this printed record.]

EXHIBIT "4"

[Printer's Note: Exhibit "4" is not reproduced here as it is the same as Exhibit "D" attached to the Complaint, and printed in full, starting at page 28 of this printed record.]

[Endorsed]: Filed Nov. 2, 1942.

[Title of District Court and Cause.]

MOTION FOR LEAVE TO AMEND COMPLAINT

Come now the plaintiffs in the above-entitled action and move the Court for an order permitting plaintiffs to amend the complaint herein, in the particulars hereinafter set forth. This motion is based upon the records and files in the above-entitled action.

PROPOSED AMENDMENT

I.

That said complaint be amended by re-forming the title thereto by adding to the present title the words, "Co-partners."

II.

That other allegations in said complaint be amended to conform to the above proposed change in title.

W. N. CUDDY,
Of Attorneys for Pltffs.

ORDER

This matter coming on before the above-entitled Court on motion of plaintiffs to amend the complaint as hereinabove stated, it is hereby

Ordered, that said complaint may be amended in accordance with the above motion.

Done by the Court at Anchorage, Alaska, this 18th day of December, 1942.

SIMON HELLENTHAL
District Judge [50]

Objected to an exception allowed deft.

S. HELLENTHAL
District Judge

[Endorsed]: Filed Dec. 18, 1942. [51]

[Title of District Court and Cause.]

MINUTE ORDER GRANTING LEAVE TO MOVE AGAINST CERTAIN PAPERS

Now at this time, on motion of Thomas M. Donohoe, Esq., of counsel for the defendants, W. N. Cuddy and George B. Grigsby, Esqs., counsel for plaintiffs, being present and consenting thereto,

It Is Ordered that defendants be, and they are hereby, granted leave to move against plaintiffs' amended complaint and reply when filed. [52]

In the District Court for the Territory of Alaska,
Third Division

No. A 2827

CHARLOTTE L. SHEELY, JOHN H. SHEELY, JOE A. SHEELY, and ROSS L. SHEELY, Copartners,

Plaintiffs,

vs.

A. T. MARTIN and ALICE M. MARTIN,

Defendants.

AMENDED COMPLAINT

Come now the plaintiffs above named and for a first cause of action against defendants allege as follows:

I.

That on the 28th day of June, 1941, the plaintiffs above named were copartners and engaged in the dairy business in the Anchorage Precinct of the Third Division of the Territory of Alaska.

II.

That during the month of June, 1941, the plaintiffs and defendants entered into oral negotiations for the purchase by the plaintiffs from the defendants, and the sale by the defendants to the plaintiffs, of the personal property comprising the whole of that certain dairy and milk distribution business conducted by the defendants under the trade name and style of "Step-and-Half Ranch", and for the leasing of the land and premises used by the de-

fendants for the conduct of the said business to the plaintiffs.

III.

That, as a result of the said oral negotiations, the plaintiffs, Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, with the defendants, entered into a "Conditional Sales Agreement", a "Lease", and a "Grazing Permit", true and correct copies of which said instruments are attached hereto, marked Exhibits "A", "B", and "C", [53] respectively, and by this reference made a part hereof the same as though set out herein in full, and that each of the said instruments was and is an integral part of the whole transaction, neither being acceptable to the plaintiffs without the others.

IV.

That by the terms of the said conditional sales agreement, the defendants agreed to sell to the plaintiffs, and the plaintiffs agreed to purchase of and from the defendants, the whole of that certain dairy and milk distribution business being then conducted by the defendants under the trade name and style of Step-And-Half Ranch, save and except the accounts receivable, but including the livestock, furniture and fixtures, farming implements and tools and motive equipment, all of which said property is set out in the inventory attached to the said conditional sales agreement, "Exhibit A", at and for the purchase price of Twenty-Eight Thousand Two Hundred Ninety-four Dollars ($28,294.00), payable $9800.00 upon the execution

of the agreement, and $308.22 on the 10th day of August, 1941, and $308.22 on the 10th day of each month thereafter until the purchase price should be paid in full, with interest at the rate of 6% per annum from July 1st, 1941, until paid.

V.

That the chief item contained in the inventory of property attached to the conditional sales agreement, "Exhibit A", was fifty-six head of cows; that said cows were figured by the parties at Three Hundred Dollars ($300.00) per head, which accounted for $16,800.00 of the total purchase price of $28,294.00; that the defendants warranted that they were the lawful owners of the said cows and had the full right, power and authority to sell the same.

VI.

That the plaintiffs, Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, on the 28th day of June, 1941, relying upon the representations of the defendants, entered into the said conditional sales agreement, "Exhibit A", executed the said lease "Exhibit B", and signed the said grazing permit, "Exhibit C", and paid to the [54] defendants the sum of $9,800.00 on account of the purchase price of the property described in the said conditional sales agreement, $200.00 on account of the said lease, and $110.00 on account of the said grazing permit, and thereafter on or about July 1st, 1941, entered into possession of the property and premises described in the said instruments, all of said acts being done for and in behalf of the above

named plaintiffs, Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely, co-partners.

VII.

That on the 28th day of June, 1941, at the insistance of the defendants, the plaintiff, Ross L. Sheely, did in writing guarantee the performance by the plaintiffs, Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, of the said conditional sales agreement and lease, a true and correct copy of which said guaranty is hereto attached, marked "Exhibit D", and by this reference made a part hereof the same as though set out herein in full.

VIII.

That the plaintiffs have performed to date of commencing this action the terms and conditions of the said conditional sales agreement, lease, grazing permit and guaranty, and, in addition to the payments alleged in Paragraph V, above, have paid to the defendants upon the said Conditional Sales agreement "Exhibit A", the sum of $1541.10 and $450.00 interest, and upon the said Lease, "Exhibit B", the sum of $1000.00, and have paid to the defendents the sum of $550.00 for their equity in a truck being purchased by the defendants from Wells Motor Company, Inc., of Anchorage, Alaska, and have paid to defendants the sum of $2000.00 for hay and grain which the defendants had on order at the time of the excution of the conditional sales agreement, and as in said conditional sales agreement provided, and have purchased additional

equipment for the dairy and made improvements upon the premises at a cost of $2513.00.

IX.

That at the time of the execution of the said Conditional Sales agreement, lease, grazing permit, and guaranty, and for a long time [55] prior thereto, a large number of the cows sold to the plaintiffs and described in the said conditional sales contract were diseased and infected with Bang's Disease or contagious abortion, which fact was well known to the defendants; and unknown to the plaintiffs; but notwithstanding such knowledge upon the part of the defendants, and with the intent to injure the plaintiffs, the defendants sold and delivered the said cows to the plaintiffs and accepted from the plaintiffs a portion of the purchase price thereof as hereinabove alleged.

X.

That all of the said cows were purchased by the plaintiffs as and for a dairy herd, which fact was well known to the defendants, and the said disease with which the said herd was and is infected renders the herd of little value for dairy purposes.

XI.

That the plaintiffs have suffered damages in the sum of Fifteen Thousand Dollars ($15,000.00) by reason of the wrongful acts and omissions of the defendants herein alleged, and will suffer irreparable damage if they are required to perform their agreements with the defendants, as herein described,

and as hereto attached and marked "Exhibits A, B, C, and D".

And for a Second Cause of Action Against the Defendants, Plaintiffs Allege: [56]

I.

That on the 28th day of June, 1941, the plaintiffs above named were copartners and engaged in the dairy business in the Anchorage Precinct of the Third Division of the Territory of Alaska.

II.

That on the 28th day of June, 1941, and for a long time prior thereto, the plaintiffs owned a large dairy herd, and operated a dairy business near the town of Palmer, in the Third Judicial Division of the Territory of Alaska, and that the cows comprising the said dairy herd were free from the disease known as Bang's Disease, or contagious abortion.

III.

That on the said date, and for a long time prior thereto, the defendants owned a large herd of cows, and operated a dairy business near the town of Anchorage, in the Third Judicial Division of the Territory of Alaska.

IV.

That on the said date, and for a long time prior thereto, the dairy herd of the defendants was infected with the said disease known as Bang's Disease, or contagious abortion, which fact was well

known to the defendants, and unknown to the plaintiffs.

V.

That on the 28th day of June, 1941, in violation of law, the defendants, without disclosing to the plaintiffs the fact that the said herd was diseased, sold to the plaintiffs fifty-six cows and one bull comprising the entire dairy herd of the defendants, and warranted that they had full right, power, and authority to sell the same.

VI.

That the plaintiffs, not knowing that the cows which they purchased from the defendants were infected with Bang's Disease, intermingled said cows with those of their own herd, and, as a result, thereof, their own dairy herd has become infected with the said disease, all to their damage in the sum of $10,000.00. [57]

Wherefore, plaintiffs pray:

1. That the Conditional Sales Agreement, "Exhibit A", described in plaintiffs first cause of action be by this court decreed illegal and void;

2. That the lease, "Exhibit B", the Grazing Permit, "Exhibit C", and the Guaranty, "Exhibit D", be rescinded, cancelled, and declared void as being part of the same transaction and based upon and supported by the illegal agreement, "Exhibit A";

3. That the plaintiffs have judgment against the defendants, and each of them, for the sum of $15,000.00 on account of their first cause of action;

4. That plaintiffs have judgment against the defendants, and each of them, for the sum of $10,000.00 on account of their second cause of action;

5. That plaintiffs have such other and further relief, as to the court may seem just and equitable in the premises;

6. That plaintiffs have judgment for their costs.

7. That the defendants be restrained and enjoined during the pendency of this cause from exercising any of the remedies provided for the defendants by the said conditional sales agreement, lease, grazing permit, and guaranty in the event of default by the plaintiffs.

W. N. CUDDY

Of Attorney for the Plaintiffs.

[58]

United States of America,
Territory of Alaska.—ss.

Ross L. Sheely being first duly sworn on oath, deposes and says: That I am one of the plaintiffs named in the foregoing amended complaint which I have read and know the contents thereof, and that the statements and allegations therein contained are true as I verily believe.

ROSS L. SHEELY

Subscribed and sworn to before me this 19th day of December, 1942.

W. N. CUDDY

Notary Public in and for Alaska.

My commission expires 8/29/45.

[Printer's Note: Exhibits "A", "B", "C" and "D", attached to the Amended Complaint, are not

reproduced here, as they are the same as Exhibits "A", "B", "C" and "D", attached to the Original Complaint, and printed in full at pages 10 to 28 of this printed record.]

[Endorsed]: Filed Dec. 21, 1942. [59]

[Title of District Court and Cause.]

REPLY

Come now the plaintiffs in the above entitled action and replying to the defendants' answer filed herein admit, deny and allege as follows:

I.

That on the 28th day of June, 1941 and at all times hereinafter mentioned, the plaintiffs above named were copartners engaged in the dairy business in the Anchorage Precinct of the Third Division of the Territory of Alaska.

II.

That the contracts set forth in defendants' answer and numbered "Exhibits 1, 2 and 3", were entered into by the said Charlotte L. Sheely, John H. Sheely and Joe A. Sheely for and in behalf of the above named plaintiffs, to wit, Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely.

Replying to defendants' answer to plaintiffs' second cause of action and affirmative defense and

counterclaim thereto plaintiffs admit, deny and allege as follows:

I.

That on the 28th of June, 1941, the plaintiffs above named were copartners and engaged in the dairy business in the Anchorage Precinct of the Third Division of the Territory of Alaska. [75]

II.

That during the month of June, 1941, the plaintiffs and defendants entered into oral negotiations for the purchase by the plaintiffs from the defendants, and the sale by the defendants to the plaintiffs, of the personal property comprising the whole of that certain dairy and milk distribution business conducted by the defendants under the trade name and style of "Step-and-Half Ranch", and for the leasing of the land and premises used by the defendants for the conduct of the said business to the plaintiffs.

III.

That as a result of said oral negotiations the plaintiffs, Charlotte L. Sheely, John A. Sheely and Joe A. Sheely, with the defendants entered into the conditional sales agreement, lease and grazing permit, true and correct copies of which said instruments are attached the original amended complaint herein and marked "Exhibits A, B, and C, and are set forth in the answer herein and designated in said answer as "Exhibits 1, 2 and 3", and by reference are hereby made a part of this reply.

That said contracts were entered into by the said

Charlotte L. Sheely, John H. Sheely and Joe A. Sheely for and in behalf of the plaintiffs named herein as copartners.

IV.

That by the terms of the said conditional sales agreement, the defendants agreed to sell to the plaintiffs, and the plaintiffs agreed to purchase of and from the defendants, the whole of that certain dairy and milk distribution business being then conducted by the defendants under the trade name and style of Step-And-Half Ranch, save and except the accounts receivable, but including the livestock, furniture and fixtures, farming implements and tools and motive equipment, all of which said property is set out in the inventory attached to the said conditional sales agreement, "Exhibit A", at and for the purchase price of Twenty-Eight Thousand Two Hundred Ninety-four Dollars ($28,294.00), payable $9800.00 upon the execution of the agreement, and $308.22 on the 10th day of August, 1941, [76] and $308.22 on the 10th day of each month thereafter until the purchase price should be paid in full, with interest at the rate of 6% per annum from July 1st, 1941, until paid.

V.

That the chief item contained in the inventory of property attached to the conditional sales agreement, "Exhibit A", was fifty-six head of cows; that said cows were figured by the parties at Three Hundred Dollars ($300.00) per head, which accounted for $16,800.00 of the total purchase price of $28,-

294.00; that the defendants warranted that they were the lawful owners of the said cows and had the full right, power and authority to sell the same.

VI.

That the plaintiffs, Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, on the 28th day of June, 1941, relying upon the representations of the defendants, entered into the said conditional sales agreement, "Exhibit A", executed the said lease, "Exhibit B", and signed the said grazing permit, "Exhibit C", and paid to the defendants the sum of $9,800.00 on account of the purchase price of the property described in the said conditional sales agreement, $200.00 on account of the said lease, and $110.00 on account of the said grazing permit, and thereafter on or about July 1st, 1941, entered into possession of the property and premises described in the said instruments.

VII.

That on the 28th day of June, 1941, at the insistance of the defendants, the plaintiff, Ross L. Sheely, did in writing guarantee the performance by the plaintiffs, Charlotte L. Sheely, John H. Sheely, and Joe A. Sheely, of the said conditional sales contract and lease, a true and correct copy of which said guaranty is attached to the amended complaint herein and marked "Exhibit D" and by this reference made a part hereof the same as though set out herein in full. [77]

VIII.

That the plaintiffs have performed to date of commencement this action the terms and conditions of the said conditional sales agreement, lease, grazing permit, and guaranty, and, in addition to the payments alleged in Paragraph V, above, have paid to the defendants upon the said Conditional Sales agreement "Exhibit A", the sum of $1541.10 and $450.00 interest, and upon the said Lease, "Exhibit B," the sum of $1000.00, and have paid to the defendants the sum of $550.00 for their equity in a truck being purchased by the defendants from Wells Motor Company, Inc., of Anchorage, Alaska, and have paid to defendants the sum of $2000.00 for hay and grain which the defendants had on order at the time of the execution of the conditional sales agreement, and as in said conditional sales agreement provided, and have purchased additional equipment for the dairy and made improvements upon the premises at a cost of $2513.00.

IX.

That at the time of the execution of the said Conditional Sales agreement, lease, grazing permit, and guaranty, and for a long time prior thereto, a large number of the cows sold to the plaintiffs and described in the said conditional sales agreement were diseased and infected with Bang's Disease or contagious abortion, which fact was well known to the defendants; and unknown to the plaintiffs; but, notwithstanding such knowledge upon the part of the defendants, and with the intent to injure the

plaintiffs, the defendants sold and delivered the said cows to the plaintiffs and accepted from the plaintiffs a portion of the purchase price thereof as hereinabove alleged.

X.

That all of the said cows were purchased by the plaintiffs as and for a dairy herd, which fact was well known to the defendants, and the said disease with which the said herd was and is infected renders the herd of little value for dairy purposes.

[78]

Replying to defendants' second counterclaim and second cross complaint, plaintiffs admit, deny and allege as follows:

I.

Plaintiffs deny each and every allegation in said second counterclaim and second cross complaint, except those allegations hereinafter specifically admitted.

II.

Plaintiffs reaffirm, reallege and adopt in this reply to defendants' said second counterclaim and second cross complaint all the allegations set forth and contained in plaintiffs' reply to defendants' answer to plaintiffs' second cause of action.

Replying to defendants' third counterclaim and third cross complaint, plaintiffs admit, deny and allege as follows:

I.

Plaintiffs reaffirm, reallege and adopt all the allegations contained and set forth in plaintiffs' reply

to defendants' answer to plaintiffs' second cause of action.

Wherefore, plaintiffs pray for judgment against the defendants on their first cause of action for the sum of Fifteen Thousand Dollars ($15,000.00); and on their second cause of action for the sum of Ten Thousand Dollars ($10,000.00); and for judgment on plaintiffs' counterclaim herein in the sum of Eighteen Thousand One Hundred Sixty-four and 10/100 Dollars ($18,164.10) and for their costs, disbursements and expenses herein had.

W. N. CUDDY

of Attorney for Plaintiffs. [79]

United States of America,
Territory of Alaska—ss.

Ross L. Sheely being first duly sworn on oath, deposes and says:

That I am one of the plaintiffs named in the foregoing Reply which I have read and know the contents thereof, and that the statements and allegations therein contained are true as I verily believe.

ROSS L. SHEELY

Subscribed and sworn to before me this 19th day of December, 1942.

[Seal] W. N. CUDDY

Notary Public in and for Alaska. My commission expires 8/29-45.

[Endorsed]: Filed Dec. 21, 1942. [80]

[Title of District Court and Cause.]

MOTION TO STRIKE

Comes now the defendants above-named and moves this Honorable Court for an order striking from the files herein plaintiffs' amended complaint in this action upon the ground and for the reason that the same does not conform to the order of this Court permitting amendment.

This motion is based upon the records and files in this action.

Dated at Anchorage, Alaska, this 21st day of December, 1942.

THOMAS M. DONOHOE &
JOHN E. MANDERS
Attorneys for Defendants.

Service of the Foregoing Motion by Receipt of Copy Thereof Acknowledged on This 21st day of December, 1942.

W. N. CUDDY
Attorney for Pltfs.

[Endorsed]: Filed Dec. 21, 1942. [81]

[Title of District Court and Cause.]

MINUTE ORDER DENYING ORDER TO STRIKE

Now at this time the defendants' motion to strike the plaintiffs' amended complaint came on regularly for hearing before the Court, the plaintiffs,

Charlotte L. Sheely and Ross L. Sheely, being present in person, and all the plaintiffs being represented by their counsel, W. N. Cuddy and George B. Grigsby, Esq., the defendants, A. T. Martin, and Alice M. Martin, being present in person and being represented by their counsel, Thomas M. Donohoe and John E. Manders, Esqs.

Whereupon, after hearing the arguments of respective counsel, the Court denied the defendants' motion to strike, to which ruling the defendants, through their counsel, except and exception allowed. [82]

[Title of District Court and Cause.]

DEMURRER TO AMENDED COMPLAINT

Come now the defendants above-named and demur to the amended complaint of the plaintiffs in the above-entitled action upon the following grounds, to-wit:

1. That the first cause of action thereof does not state facts sufficient to constitute a cause of action.

2. That the second cause of action thereof does not state facts sufficient to constitute a cause of action.

3. That several causes of action have been improperly united.

THOMAS M. DONOHOE &
JOHN E. MANDERS
Attorneys for Defendants

Service of the Foregoing Demurrer by Receipt of Copy Thereof Acknowledged on This 21st day of December, 1942.

W. N. CUDDY
Attorney for the Pltfs.

[Endorsed]: Filed Dec. 21, 1942. [83]

[Title of District Court and Cause.]

MINUTE ORDER OVERRULING DEMURRER

Now at this time the defendants' demurrer to plaintiffs' amended complaint came on regularly for hearing before the Court, the plaintiffs, Charlotte L. Sheely and Ross L. Sheely, being present in person, and all the plaintiffs being represented by their counsel, W. N. Cuddy and George B. Grigsby, Esqs., the defendants, A. T. Martin and Alice M. Martin being present in person and being represented by their counsel, Thomas M. Donohoe and John E. Manders, Esqs.

Whereupon, it being stated that this demurrer was similar to the demurrer previously filed against the plaintiffs' original complaint, the Court overruled the defendants' demurrer to plaintiffs' amended complaint, to which ruling the defendant, through their counsel, except and exception allowed. [84]

[Title of District Court and Cause.]

MINUTE ORDER GRANTING DEFENDANTS LEAVE TO PLEAD ESTOPPEL

Now at this time, on motion of Thomas M. Donohoe, Esq., of counsel for defendants, W. N. Cuddy and George B. Grigsby, Esqs., counsel for plaintiffs, being present and consenting thereto.

It Is Ordered that the defendants' answer may go to plaintiffs' amended complaint and that defendants may also have a right to plead estoppel.

[85]

[Title of District Court and Cause.]

TRIAL BY JURY CONTINUED

Now came the Trial Jury who, on being called, each answered to his or her name, came the respective parties and the respective counsel, as heretofore, and the trial of this cause was resumed.

At this time it was stipulated that the respective parties join in the reporting of this cause.

Opening statement to the Jury was had by W. N. Cuddy, Esq., for and in behalf of the plaintiffs.

Statement to the Jury was had by Thomas M. Donohoe, Esq., for and in behalf of the defendant.

Dr. Earl Francis Graves, being first duly sworn, testified for and in behalf of the plaintiffs.

At this time the defendants, through their counsel, objected to the testimony of the witness Dr. Earl Francis Graves, objection overruled, to which ruling the defendants except and exception allowed.

At this time the defendants, through their counsel, objected to all the evidence adduced in this case, objection overruled, to which ruling the defendants except and exception allowed.

At 11:50 o'clock A.M., the Court duly admonished the Trial Jury and continued the trial of this cause until 2:00 o'clock P.M. this date. [86]

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This cause came on for hearing on the 21st day of December, 1942 before the above entitled court sitting at Anchorage, Alaska, and the plaintiffs appearing in person and by their attorneys, Warren N. Cuddy and George B. Grigsby, the defendants appearing in person and by their attorneys, T. M. Donohoe and John E. Manders.

A jury having been empaneled and sworn, witnesses were sworn and testified on behalf of the plaintiffs and defendants and thereafter, both parties having stipulated that their causes of action were in equity and that the jury be discharged and the cause be determined by the court, accordingly said jury was excused and the court having heard the testimony and being fully advised in the premises, now makes the following Findings of Fact and Conclusions of Law.

FINDINGS OF FACT

I.

That on the 26th day of June, 1941 plaintiffs were copartners and engaged in the dairy business in the Anchorage Precinct, Third Division of the Territory of Alaska.

II.

That on said 26th day of June, 1941 the plaintiffs Charlotte L. Sheely, John H. Sheely and Joe A. Sheely, on behalf of said copartnership, entered into certain contracts with the defendants constituting a conditional sales agreement, a lease and an assignment of a grazing [87] permit; that by the terms of said conditional sales agreement the plaintiffs purchased from the defendants that certain dairy and milk distribution business being then conducted by the defendants in the Anchorage Precinct, Third Division, Territory of Alaska, under the trade name and style of "Step-And-Half Ranch", said purchase including the *life* stock and certain personal property then on said Ranch; that the aforesaid conditional sales agreement, lease and assignment of grazing permit were interdependent agreements constituting one transaction; that true and correct copies of said instruments are attached to the amended complaint herein and marked Exhibits "A", "B" and "C" respectively.

III.

That pursuant to said agreements hereinbefore described the plaintiffs paid to the defendants certain sums of money as follows, to wit:

$9800.00 on the execution of said conditional sales agreement

308.22 on the 10th day of October, 1941
308.22 on the 10th day of November, 1941
308.22 on the 10th day of December, 1941
308.22 on the 10th day of August, 1941
308.22 on the 10th day of September, 1941

That on said lease agreement the plaintiffs paid to the defendants as follows:

$200.00 on the 1st day of July, 1941
200.00 on the 1st day of August, 1941
200.00 on the 1st day of September, 1941
200.00 on the 1st day of October, 1941
200.00 on the 1st day of November, 1941
200.00 on the 1st day of December, 1941

That pursuant to said conditional sales agreement plaintiffs paid to defendants on and before December 10, 1941 the sum of $450.00 interest which became due under said agreement.

That in consideration for the assignment of said grazing permit the plaintiffs paid to defendants on August 19, 1941 the sum of $110.00.

That at various times prior to January, 1942 the plaintiffs paid for permanent improvements to said dairy ranch and for durable supplies and equipment the sum of $1766.85; that the payments and expenditures [88] set forth in this paragraph amount to the sum of $14,867.95.

IV.

That pursuant to said conditional sales agreement, lease and grazing permit, the plaintiffs on the 1st

day of July, 1941 entered into the possession of said Step-And-Half Ranch and dairy business and the cows and personal property thereon, mentioned in said agreement, and proceeded to conduct a dairy business; that at the time said plaintiffs entered into said agreements and at the time said plaintiffs entered into possession of said premises, and for a long time prior thereto, a large number of the cows sold to the plaintiffs and described in the said conditional sales contract were diseased and infected with Bang's Disease or contagious abortion, which fact was well known to the defendants and unknown to the plaintiffs; that notwithstanding such knowledge upon the part of the defendants and without disclosing the same to the plaintiffs, the defendants sold and delivered the said premises and live stock thereon to the plaintiffs and accepted from the plaintiffs a portion of the purchase price thereof as hereinabove alleged.

V.

That on account of said cattle being diseased and infected with Bang's disease or contagious abortion, a great number thereof, to wit, 36, became useless for dairy purposes and plaintiffs were compelled on that account to slaughter and sell the same for beef, from which sale the plaintiffs derived the sum of $4472.20; that 6 of said cows died on account of said disease and there are 14 cows and one bull left of the original herd, on the premises.

That the plaintiffs have also now on said premises 12 cows which were brought from a ranch in Palmer

and were intermingled with the original herd on the Step-And-Half Ranch; that these said cows are now the property of the plaintiffs.

And from the foregoing facts the Court deduces the following Conclusions of Law. [89]

CONCLUSIONS OF LAW

I.

That the aforesaid conditional sales agreement, lease and grazing permit constituted one transaction and were illegal, against public policy and prohibited by Section 2 of Chapter 55 of the Session Laws of Alaska, 1919 (Sec. 626, Compiled Laws of Alaska, 1933).

II.

That the plaintiffs are entitled to recover from the defendants the sum of $14,867.95, being moneys paid and expended as set forth in paragraph III of the Findings of Fact herein, together with interest on the various payments and expenditures from the time made, amounting in all to the sum of $16,-091.89; that from this sum the defendants are entitled to deduct in the sum of $4472.20, leaving the balance due from defendants to plaintiffs of the sum of $11,619.69, for which plaintiffs are entitled to judgment against the defendants.

III.

That the plaintiffs are entitled to dispose of the 12 cows now on the Step-And-Half Ranch belonging to them, either by slaughtering or otherwise as may be permitted by law.

IV.

That said conditional sales agreement, lease agreement and assignment of grazing permit should be rescinded.

V.

That the defendants are entitled to immediate possession of the said premises constituting the Step-And-Half Ranch and the live stock and personal property thereon, except the said 12 cows belonging to plaintiffs; to the possession of the land described in the said lease agreement and to the use of the area described in said grazing permit.

Let a decree be entered accordingly.

Dated at Anchorage, Alaska, this 4th day of January, 1943.

SIMON HELLENTHAL,
District Judge.

To each of the above the defts. object and an exception is allowed them.

SIMON HELLENTHAL,
District Judge. 1/4/43 [90]

[Endorsed]: Filed Jan. 4, 1943. [91]

In the District Court for the Territory of Alaska,
Third Division

No. A 2827

CHARLOTTE L. SHEELY, JOHN H. SHEELY, JOE A. SHEELY, and ROSS L. SHEELY, Copartners,

Plaintiffs,

vs.

A. T. MARTIN and ALICE M. MARTIN,

Defendants.

DECREE

This cause coming on for trial on the 21st day of December, 1942, before the above entitled court, the plaintiffs appearing in person and by their attorneys, Warren N. Cuddy and George B. Grigsby, and the defendants appearing in person and by their attorneys, T. M. Donohoe and John E. Manders; A jury having been empaneled and sworn, witnesses having been sworn and testified on behalf of plaintiffs and defendants and at the conclusion of the testimony both parties having stipulated that their causes of action were in equity and that they be determined by the court, thereupon, the jury having been excused and the court having determined the issues raised by the pleadings and being fully advised in the premises, having made findings of fact and conclusions of law, now therefore,

It Is Ordered, Adjudged and Decreed:

I.

That the plaintiffs have and recover from the defendants the sum of $11,619.69 with interest according to law from the date hereof.

II.

That plaintiffs sell for beef or otherwise dispose of as may be permitted by law the 12 cows belonging to plaintiffs and now on the premises known as the "Step-And-Half Ranch" near Anchorage, Alaska, and retain the proceeds thereof. [92]

III.

That the conditional sales agreement, agreement for lease and assignment of grazing permit, copies of which are annexed to the amended complaint herein and marked Exhibits "A", "B" and "C" respectively, be, and the same are declared illegal and are hereby rescinded.

IV.

That the defendants have possession of the leased premises known as the "Step-And-Half Ranch", the live stock and personal property thereon, except 12 cows belonging to plaintiffs; that defendants have possession of the land described in said grazing permit.

V.

That the plaintiffs have and recover their costs and disbursements herein amounting to the sum of

.....

Dated this 4th day of January, 1943.

SIMON HELLENTHAL,
District Judge.

To the foregoing the defendants object and an exception is allowed defendants.

SIMON HELLENTHAL,
District Judge. 1/4/43

[Endorsed]: Filed Jan. 4, 1943. [93]

[Title of District Court and Cause.]

MOTION FOR A NEW TRIAL

Come now the defendants above named and move this honorable court for an order setting aside and vacating the judgment heretofore entered in the above entitled action in favor of plaintiffs and against the defendants, and feeling aggrieved by such judgment move that a new trial of said action be granted to said defendants for the following causes alleged by defendants as materially effecting their substantial rights and the rulings of the court which were prejudicial to their substantial rights, to wit:

Errors in law occurring at the trial and excepted to by the defendants;

1. The court erred in overruling the demurrer of defendants to the complaint of plaintiffs on file herein.

2. The court erred in permitting and allowing the complaint of plaintiffs to be amended by setting

forth a partnership including plaintiff, Ross L. Sheely.

3. The court erred in denying defendants' motion to strike the amended complaint of plaintiffs from the files in said action.

4. The court erred in overruling the demurrer of defendants to the amended complaint of plaintiffs on file in said action.

5. The court erred in admitting the testimony of Dr. Earl F. Graves. [94]

6. The court erred in overruling the objection of defendants to all of the testimony on behalf of the plaintiffs in said action.

7. The court erred in admitting in evidence plaintiffs' Exhibit "C", a Bangs disease test report, Serial No. 1388, dated March 7, 1941.

8. The court erred in denying defendants' motion to strike plaintiffs' Exhibit "C" from the files in said action.

9. The court erred in ordering two words, "butchered", from the face of Exhibit "C" removed.

10. The court erred in refusing to strike out the testimony of Ross L. Sheely in regard to moneys expended by him, he not being a partner to the contracts the subject matter of said action.

11. The court erred in refusing to strike out the testimony of Ross L. Sheely as to moneys paid by him on the ground that no partnership had been shown to exist between all of the plaintiffs in said action.

12. The court erred in refusing to strike the answer of Ross L. Sheely in response to court's inquiry as to moneys expended by him for improvements and supplies as incompetent and not limited in time to the date of the commencement of said action.

13. The court erred in denying defendants' motion at the close of plaintiffs' case to grant a non-suit on the ground that the amended complaint did not state facts sufficient to constitute a cause of action.

14. The court erred in denying defendants' motion at the close of plaintiffs' case to grant a non-suit on the ground that plaintiffs had not introduced sufficient evidence to sustain the allegations of their complaint.

15. The court erred in again denying defendants' motion for non-suit at the close of plaintiffs' case on the ground that plaintiffs had not introduced sufficient evidence to sustain the allegations of their complaint.

16. The court erred in again denying defendants' motion to [95] grant a non-suit on the ground that the amended complaint did not state facts sufficient to state a cause of action.

17. The court erred in permitting witness Ross L. Sheely to explain the meaning and operations of the agreements, Exhibits "A", "B" and "C", he, the said witness not being a party to any of said agreements.

18. The court erred in denying to defendants the

right to introduce testimony bearing upon the increase of calves in the dairy herd of defendants.

19. The court erred in denying to defendants the right to introduce testimony and the amount of money received from the sale of milk from the defendants' herd of cows.

20. The court erred in permitting witness Ross L. Sheely to testify as to moneys expended by him under the contracts and agreements, Exhibits "A", "B" and "C", he not being a party to any of said contracts or agreements, Exhibits "A", "B" and "C".

21. The court erred in permitting witness Ross L. Sheely to testify as to expenditures by him, no partnership being shown of which said witness was a partner.

22. The court erred in permitting Charlotte Sheely, one of the plaintiffs, to testify that she signed the agreements and contracts, Exhibits "A", "B" and "C" on behalf of her copartners, no copartnership having been shown and the Exhibits "A", "B" and "C" do not show or refer to a partnership.

23. The court erred in permitting John H. Sheely, one of the plaintiffs, to testify that he signed the agreements and contracts, Exhibits "A", "B" and "C" on behalf of his copartners, no copartnership having been shown and the Exhibits "A", "B" and "C" do not show or refer to a partnership.

24. The court erred in overruling the objections of defendants' to the questions in regard to para-

graph VIII of the defendants' answer asked of witness A. T. Martin on cross-examination by plaintiffs. [96]

25. The court erred in signing and filing the findings of fact and conclusions of law in said action and in finding and without limiting by specific designation findings of fact I, II, III, IV and V of the findings of fact.

And the court erred in finding as conclusions of law therefrom paragraphs I, II, III and IV of the conclusions of law.

26. The court erred in signing and filing its decree based upon said findings of fact and conclusions of law and decreeing that plaintiffs have and recover from the defendants the sum of $11,619.69 with interest according to law from date, January 4, 1943.

That the conditional sales agreement, agreement for leases and assignment of grazing permit, copies of which are annexed to the amended complaint in said action and marked Exhibits "A", "B" and "C" respectively, be and the same are declared illegal and are rescinded.

That plaintiffs have and recover their costs and disbursements in said action.

28. The court erred in applying the rule of damages for the destruction of thirty-six cows of the Martin dairy herd amounting to the sum of $4,472.20, whereas, the rule of damages to be applied should be the values of each of said cows of said dairy herd for dairy purposes, and that the rule of damages should be the replacement value of

said cows in a sum of not less than $300.00 per head, amounting to a sum of not less than $10,800.00.

Wherefore, defendants move said court to grant a new trial in the above entitled action.

Dated this 23d day of January, 1943.

THOMAS M. DONOHOE,
JOHN E. MANDERS,
Attorneys for Defendants. [97]

Service acknowledged by receipt of a copy hereof this 23d day of January, 1943.

W. N. CUDDY,
GEO. GRIGSBY,
By W. N. CUDDY,
Attorneys for Plaintiffs.

[Endorsed]: Filed Jan. 23, 1943. [98]

[Title of District Court and Cause.]

MINUTE ORDER OVERRULING MOTION FOR NEW TRIAL

This cause having come on regularly for hearing before the Court on the 15th day of April, 1943 on the defendants' motion for new trial, the plaintiffs being represented by W. N. Cuddy and George B. Grigsby, Esq., of their counsel, and the defendants being represented by Thomas M. Donohoe and John E. Manders, of their counsel, and the Court having heard the arguments of respective counsel and thereafter having granted counsel ten

days in which to prepare and submit briefs, and now on this day the Court having considered the briefs submitted by respective counsel and being fully and duly advised in the premises,

It Is Ordered that the defendants' motion for new trial be, and the same is hereby, overruled, to which ruling the defendants, through their counsel, except and an exception allowed. [99]

[Title of District Court and Cause.]

PETITION FOR ALLOWANCE OF APPEAL

To the Honorable Simon Hellenthal, Judge of the District Court for the Third Division, Territory of Alaska:

Your petitioners, A. T. Martin and Alice M. Martin, respectfully show:

I.

Petitioners are the defendants in the above entitled cause.

II.

A final judgment was entered in the above entitled cause against petitioners and in favor of plaintiffs, on January 4, 1943.

III.

A motion for new trial of the above cause was filed in the above entitled action on January 23, 1943, and thereafter, and on the 3rd day of June, 1943 said motion for new trial was denied.

Wherefore, petitioners pray that an appeal may be allowed from said judgment to the United States Circuit Court of Appeals for the Ninth Circuit, and in connection with this petition petitioners present herewith their assignment of errors.

Petitioners further pray that a supersedeas may be granted herein pending the final disposition of the cause, and that the [100] amount of surety may be fixed by the order allowing the appeal.

Dated August 24th, 1943.

THOMAS M. DONOHOE,
JOHN E. MANDERS,
Attorneys for defendants.

[Endorsed]: Filed Aug. 24, 1943. [101]

[Title of District Court and Cause.]

ASSIGNMENT OF ERRORS

Now come defendants and appellants herein and file the following assignments of error upon which they will rely in the prosecution of the appeal to the United States Circuit Court of Appeals for the Ninth Circuit, from the final decree made and entered in this cause on the 4th day of January, 1943 by the above entitled court as follows, to-wit:

1. The court erred in overruling the demurrer of defendants to the complaint of the plaintiffs on file herein upon the grounds that the same does not state facts sufficient to constitute a cause of action, which ruling was duly excepted to by the defendants herein and exception allowed.

2. The court erred in granting the motion for leave to amend complaint by the plaintiffs to incorporate therein that plaintiffs were a partnership including plaintiff Ross L. Sheely, the granting of which order was duly excepted to and exception allowed.

3. The court erred in denying defendants motion to strike plaintiffs' amended complaint upon the ground that the same did not conform to the order of the court permitting amendment, which was duly excepted to and exception allowed.

4. The court erred in overruling the demurrer to plaintiffs' [102] amended complaint upon the grounds that the same did not state facts sufficient to constitute a cause of action, which order was duly excepted to and exception allowed.

5. The court erred in denying defendants' objection to any testimony in support of plaintiffs' amended complaint, as shown by the objection to the testimony of plaintiffs' witness Earl Francis Graves, as follows:

"Q. By Mr. Cuddy: I will ask you whether or not during the month of April, 1941 you examined the dairy herd of A. T. Martin?

Mr. Donohoe: Objected to—the first cause of action does not state facts sufficient to constitute a cause of action, and the second cause of action does not state a cause of action and they have been improperly united.

Court: Motion overruled. Exception granted.

Donohoe: That will go to all this evidence. We object to the testimony of this witness, as to the

examination of the herd—it cannot vary the terms of the contract Exhibit "A"—the conditional sales contract involved herein.

Court: Motion overruled. Exception allowed."

The witness was then permitted to testify as to the condition of the herd as to Bang's disease.

6. The court erred in denying motion for nonsuit made by the defendants at the close of plaintiffs' case upon the grounds that the complaint does not state facts sufficient to constitute a cause of action, and upon the further grounds that there is not sufficient evidence to sustain the allegations of plaintiffs' complaint, to which ruling defendants excepted and exception was allowed.

7. The court erred in dismissing the jury and considering this cause as one of an equitable nature, over the objection of the defendants, to which ruling the defendants excepted and the exception was allowed. [103]

8. The court erred in refusing to allow defendants' motion for a nonsuit at the close of the trial of this action, upon the grounds that the complaint does not state facts sufficient to constitute a cause of action and that there is not sufficient evidence to sustain the allegations of plaintiffs' complaint, to which ruling defendants excepted and exception was allowed.

9. The court erred in overruling defendants' objection to the introduction of plaintiffs' Exhibit "C" introduced on the redirect examination of Earl Francis Graves, as follows:

"Donohoe: Object to the offer, it is too remote and not pertaining to the issues in this case.

Court: Objection overruled. Exception allowed."

The offer is received and marked Plaintiffs' Exhibit "C", being a report dated March 7, 1941.

Exhibit "C" being a record of the condition of Mr. Sheely's herd at Palmer, Alaska was then received.

10. The court erred in refusing to strike plaintiffs' Exhibit "C" introduced on the redirect examination of Earl Francis Graves, as follows:

"Q. By Mr. Donohoe: Are you sure that paper is the same as you prepared it on March 7, 1941, did you write that on there yourself?

A. No, that has been put on later.

Donohoe: We move to strike.

Court: I think the writing on the side should be stricken from that exhibit.

Donohoe: We move to strike the exhibit.

Court: The writing may be taken off.

Donohoe: Exception.

Court: Exception allowed. * * * * *

Donohoe: In order to keep the record straight we have to show what is on that exhibit.

Court: The record may show butchered was written on in two places after the report was made. The Court ruled that they [104] may be stricken.

Donohoe: Exception. The exhibit is not as originally prepared and will have undue influence upon the jury in the trial of this case.

Court: No objection was made at the time the

exhibit was offered on account of those words being there. Exception allowed."

The exhibit was the same exhibit "C", being a record of the condition of Mr. Sheely's herd of cows at Palmer, Alaska.

11. The court erred in overruling defendants' objection to questions asked plaintiffs' witness Ross L. Sheely on direct examination, as follows:

"Q. By Mr. Cuddy: I notice in Exhibits "A", "B", and "C" that your name is not on the list, not a signature to it but as a guaranty, will you explain to the jury how that situation arose?

Donohoe: Objected to as incompetent, the pleadings and exhibits speak for themselves.

Court: Objection overruled. Exception granted."

Mr. Sheely was then permitted over objection to testify that he was operating as a copartner with the other members of the family and his reasons for having a copartnership, contrary to the original agreements entered into between plaintiffs and defendants herein.

12. The court erred in sustaining plaintiffs' objection to the question asked plaintiffs' witness Ross L. Sheely on cross-examination, as follows:

"Q. By Mr. Donohoe: How much have you received from the butchered calves?

Grigsby: Objected to as immaterial.

Court: I will not go into the increase. Exception allowed.

Q. How much have you received from the sale of milk from these cows.

Grigsby: Objected to. [105]

Court: Objection sustained. Exception granted."

The court refused to permit defendants to prove the value of the milk products sold by plaintiffs, derived from said dairy herd and also refused to permit defendants to prove the value of the calves born to said dairy cows and received by plaintiffs, and the court refused to permit defendants to prove the value of other products sold from the ranch premises and received by plaintiffs.

13. The court erred in refusing to grant the motion of the defendants to strike the testimony of plaintiffs' witness Ross L. Sheely as to improvements made to the premises and as to what was a reasonable value for rental of the land, contrary to the amount agreed upon in the written lease, and as to the individual value of cows, and money spent by the witness Ross L. Sheely, as follows:

"Donohoe: I couldn't very well object to the questions of the Court, but if your Honor please I move to strike the answers of the witness as incompetent, irrelevant and immaterial.

Court: Motion denied.

Donohoe: I also object to the testimony of this witness as to monies spent by this witness as incompetent. This witness was not a party to this contract.

Court: Was this money paid under the contract?

A. Yes, sir.

Q. And you know it was paid under the contract? A. Yes, sir.

Court: Motion overruled. Exception allowed.

Donohoe: He testified he paid it.

Grigsby: On whose behalf was this money paid —on your part or on the part of the co-partnership?

Donohoe: Object, there is no mention of a co-partnership in the agreement. [106]

Court: You may have an exception."

14. The court erred in overruling defendants' objection to the question asked plaintiffs' witness Charlotte Sheely on direct examination, as follows:

"Q. By Mr. Cuddy: Covering the purchase of cattle on the Martin ranch and a lease of the property on behalf of whom were those three signatures?

Donohoe: Object as incompetent. The papers speak for themselves.

Court: She may testify. Exception allowed.

A. I signed it for the copartners, the four, Mr. Sheely, myself, Jack and Joe."

15. The court erred in overruling defendants' objection to the question asked plaintiffs' witness John H. Sheely on direct examination, as follows:

"Q. By Mr. Cuddy: And in whose benefit did you sign such instrument?

Donohoe: Object to the question.

Court: Objection overruled.

Q. For whose benefit did you sign that agreement?

Donohoe: Object as incompetent, the papers speak for themselves.

A. Well, I signed it on behalf of—we were

planning a partnership, we were going to work it on shares."

16. The court erred in finding:

(a) As in its first findings of fact, that on the 26th day of June, 1941 plaintiffs were copartners;

(b) As in its second findings of fact, that on said 26th dayof June, 1941 plaintiffs Charlotte L. Sheeley, John H. Sheeley and Joe A. Sheeley "on behalf of said partnership," entered into certain contracts, copies of which are attached to the amended complaint marked Exhibits "A", "B" and "C"; [107]

(c) As in its third findings of fact, "That at various times prior to January, 1942 the plaintiffs paid for permanent improvements to said dairy ranch and for durable supplies and equipment the sum of $1766.85;****"

(d) As in its fourth findings of fact, "That at the time said plaintiffs entered into said agreements and at the time said plaintiffs entered into possession of said premises, and for a long time prior thereto, a large number of the cows sold to the plaintiffs and described in the said conditional sales contract were diseased and infected with Bang's Disease or contagious abortion, which fact was well known to the defendants and unknown to the plaintiffs; that notwithstanding such knowledge upon the part of the defendants and without disclosing the same to the plaintiffs, the defendants sold and delivered the said premises and live stock thereon to the plaintiffs and accepted from the plaintiffs a portion of the purchase price thereof as hereinabove alleged."

(e) As in its fifth findings of fact, that 36 of said cattle "became useless for dairy purposes and plaintiffs were compelled on that account to slaughter and sell the same for beef, from which sale the plaintiffs derived the sum of $4472.20; that 6 of said cows died on account of said disease and there are 14 cows and one bull left of the original herd, on the premises."

And to each of which said findings defendants excepted and said exceptions were allowed.

17. The court erred in forming its conclusions of law, as follows:

(a) Conclusion of law No. I: "That the aforesaid conditional sales agreement, lease and grazing permit constituted one transaction and were illegal, against public policy and prohibited by Section 2 of Chapter 55 of the Session Laws of Alaska, 1919 (Sec. 626, Compiled Laws of Alaska, 1933)". [108]

(b) Conclusion of Law No. II: "That the plaintiffs are entitled to recover from the defendants the sum of $14,867.95, being moneys paid and expended as set forth in paragraph III of the Findings of Fact herein, together with interest on the various payments and expenditures from the time made, amounting in all to the sum of $16,091.89; that from this sum the defendants are entitled to deduct in the sum of $4472.20, leaving the balance due from defendants to plaintiffs of the sum of $11,619.69, for which plaintiffs are entitled to judgment against the defendants."

(c) Conclusion of Law No. III: "That the plaintiffs are entitled to dispose of the 12 cows now

on the Step-And-Half Ranch belonging to them, either by slaughtering or otherwise as may be permitted by law."

(d) Conclusion of Law No. IV: "That said conditional sales agreement, lease agreement and assignment of grazing permit should be rescinded."

(e) Conclusion of Law No. V: "That the defendants are entitled to immediate possession of the said premises constituting the Step-And-Half Ranch and the live stock and personal property thereon, except the said 12 cows belonging to plaintiffs, to the possession of the land described in the said lease agreement and to the use of the area described in said grazing permit."

To each of which conclusions of law defendants excepted and said exceptions were allowed.

18. The court erred in rendering its decree for the plaintiffs herein. The court's error in this regard was based upon the following errors of the court occurring during the trial of the case: All of the errors herein assigned, to-wit: Assignments of Error 1 to 17 inclusive.

WHEREFORE, defendants and appellants pray that the judgment in the above entitled cause be reversed and the cause remanded, [109] with instructions to the trial court as to further proceedings therein, and for such other and further relief as may be just in the premises.

Dated, this 24th day of August, 1943.

THOMAS M. DONOHOE
JOHN E. MANDERS
Attorneys for defendants and
Appellants.

[Endorsed]: Filed Aug. 24, 1943. [110]

[Titleof District Court and Cause.]

ORDER ALLOWING APPEAL AND SUPERSEDEAS

The petition of A. T. Martin and Alice Martin, defendants in the above entitled cause, for an appeal from the final judgment rendered therein, is hereby granted, and the appeal is allowed, and upon petitioners filing a bond in the sum of $12,500.00 with sufficient sureties and conditioned as required by law, the same shall operate as a supersedeas of the judgment made and entered in the above cause and shall suspend and stay all further proceedings in this court until the termination of said appeal by the United States Circuit Court of Appeals for the Ninth Circuit.

Dated: August 24th, 1943.

SIMON HELLENTHAL
District Judge

[Endorsed]: Filed Aug. 24, 1943. [111]

[Title of District Court and Cause.]

CITATION ON APPEAL

To the Plaintiffs, Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely, Copartners, and to their attorneys Warren N. Cuddy and George B. Grigsby:

You and each of you are hereby cited and admonished to be and appear in the United States Circuit Court of Appeals for the Ninth Circuit, to be held at San Francisco, in the State of California, thirty (30) days from the date of the within citation, pursuant to the order allowing appeal on file in the Clerk's Office of the District Court for the Territory of Alaska, Third Division, and in that certain action pending in said United States District Court entitled, "Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely, Copartners, plaintiffs, vs. A. T. Martin and Alice M. Martin, defendants", being Number A-2827 on the files of said District Court, and wherein A. T. Martin and Alice M. Martin are appellants and you are appellees, to show cause, if any there be, why the judgment rendered against said A. T. Martin and Alice M. Martin should not be corrected and why speedy justice should not be done to the parties in that behalf.

Witness the Honorable Simon Hellenthal, District Judge for the Territory of Alaska, Third

Division, this 24th day [112] of August, 1943, and of the independence of the United States the 168th.

SIMON HELLENTHAL
Judge of the District Court
for the Territory of
Alaska, Third Division.

Attest:
[Seal] M. E. S. BRUNNELLE
Clerk of said Court.

[Endorsed]: Filed Aug. 24, 1943. [113]

[Title of District Court and Cause.]

SUPERSEDEAS AND COST BOND

Know All Men By These Presents: That we, A. T. Martin and Alice M. Martin, as principals, and Arthur F. Waldron and Edward McElligott as sureties, are held and finally bound unto Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely, Copartners, in the full and just sum of Twelve Thousand Five Hundred Dollars ($12,500.00) to be paid to the said Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely, Copartners, their heirs, executors, administrators, successors and assigns, to which payment well and truly to be made we bind ourselves, our heirs, executors, administrators, successors or assigns jointly and severally by these presents. Sealed with our seals and dated this 24th day of August, 1943.

Whereas, lately at the October 1942 term of the District Court for the Territory of Alaska, Third Division in a suit pending in said court between Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely, Copartners, plaintiffs, and A. T. Martin and Alice M. Martin, defendants, a judgement was rendered against the said A. T. Martin and Alice M. Martin, defendants, at the said October Term of Court, and the said A. T. Martin and Alice M. Martin, defendants, have petitioned for and been allowed an appeal to the United States Circuit Court of Appeals for the Ninth Circuit and a citation has been issued [114] directed to the said Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely, Copartners, citing them to appear in said court at San Francisco, California, thirty (30) days from and after the date of such citation.

Now the condition of the above obligation is such that if the said A. T. Martin and Alice M. Martin shall prosecute the said appeal to effect and answer all damages and costs if they fail to make good their plea, then the above obligation to be void, otherwise to remain in full force and effect.

[Seal] A. T. MARTIN
[Seal] ALICE M. MARTIN
Principals
[Seal] EDWARD McELLIGOTT
[Seal] ARTHUR F. WALDRON
Sureties

United States of America,
Territory of Alaska—ss:

Arthur F. Waldron and Edward McElligott being first duly sworn on oath, depose and say, each for himself and not one for the other: I am one of the sureties on the foregoing bond; that I am a resident of the Territory of Alaska owning property therein; I am not a counsellor or attorney at law, marshal, clerk of any court or other officer of any court; that I am worth the sum of Twelve Thousand Five Hundred Dollars ($12,500.00), specified in the foregoing undertaking, exclusive of property exempt from execution and over and above all just debts and liabilities.

EDWARD McELLIGOTT
ARTHUR F. WALDRON

Subscribed and sworn to before me this 24th day of August, 1943.

[Seal] JOHN E. MANDERS
Notary Public for Alaska. My Commission expires 9/6/45.

The foregoing bond and undertaking is approved and allowed this 24th day of August, 1943.

SIMON HELLENTHAL
District Judge [115]

[Endorsed]: Filed Aug. 24, 1943. [116]

[Title of District Court and Cause.]

ACKNOWLEDGMENT OF SERVICE

The undersigned, attorneys for plaintiffs herein, hereby acknowledge receipt of true copies of each of the following documents, to-wit:

1. Petition for allowance of appeal.
2. Assignment of errors.
3. Order allowing appeal and supersedeas.
4. Supersedeas and cost bond.
5. Order extending time for settling bill of exceptions.
6. Citation on appeal.

Dated this 25th day of August, 1943.

W. N. CUDDY
GEO. B. GRIGSBY
Attorneys for Plaintiffs.

[Endorsed]: Filed Aug. 25, 1943. [117]

[Title of District Court and Cause.]

ORDER EXTENDING TIME FOR SETTLING BILL OF EXCEPTIONS

This matter coming on for hearing upon the application of the defendants A. T. Martin and Alice M. Martin, requesting sixty (60) days additional time to prepare and file the record on appeal in the above-entitled cause, and to settle the bill of exceptions; it is hereby

Ordered, that the defendants have sixty (60) days additional time, to-wit, until the 24th day of October, 1943, within which to prepare, file, or have

approved, the record and bill of exceptions in the above entitled cause.

Made and Ordered Entered at Anchorage, Alaska, this 24th day of August, 1943.

SIMON HELLENTHAL
District Judge

[Endorsed]: Filed Aug. 24, 1943. [118]

[Title of District Court and Cause.]

STATEMENT OF EVIDENCE AND BILL OF EXCEPTIONS

This cause came on for trial before the Honorable Simon Hellenthal, Judge of the above entitled court, at a session of said court held at Anchorage, Alaska, in the Third Judicial Division of said Territory on the 19th day of December, 1942; the plaintiffs appearing in person and by their attorneys W. N. Cuddy and George Grigsby; the defendants appearing in person and by their attorneys John E. Manders and Thomas M. Donohoe.

Whereupon a jury was duly selected, empaneled and sworn. Proceedings were then had in said cause as shown by the statement of the evidence duly approved, settled and certified as correct and complete, as follows:

STATEMENT OF TESTIMONY

In order to sustain the issues in the above entitled cause the plaintiffs called as a witness in their behalf

EARL FRANCIS GRAVES

who being first duly sworn, testified as follows:

My name is Earl Francis Graves. I live at Palmer, Alaska. I am Territorial veterinarian. I have held that position since December of 1940. I graduated in veterinary in 1927 and have followed my profession continuously since that date. It is my work as Territorial veterinarian to examine all dairy and live stock for contagious diseases at least once a year if there are funds. These diseases specifically include tuberculosis and [119] contagious abortion or Bang's disease.

Q. I will ask you whether or not during the month of April, 1941 you examined the dairy herd of A. T. Martin?

Mr. Donohoe: Objected to—the first cause of action does not state facts sufficient to constitute a cause of action, and the second cause of action does not state a cause of action and they have been improperly united.

Court: Motion overruled. Exception granted.

Donohoe: That will go to all this evidence. We object to the testimony of this witness, as to the examination of the herd—it cannot vary the terms of the contract Exhibit "A"—the conditional sales contract involved herein.

Court: Motion overruled. Exception allowed.

A. Yes, I did.

On April 22, 1941, I examined the herd of Mr. Martin—no tuberculosis re-actors; I did find 21 with contagious abortion and 8 suspect re-actors

(Testimony of Earl Francis Graves.)

and the rest were clean. The number of clean cattle would be the difference between 21 and 8, and the total of 54 that I examined for tuberculosis. Fifty-four animals were examined by me at that time. This examination was being made by myself in the City of Anchorage. Mr. Morley of the Territorial Board of Health and Mr. Martin and myself were present at the time of the examination. As a custom, I make the hotels in each community my office and I ran the bloods down in the hotel, it happened to be the Parsons. I found so many re-actors that I thought Martin should see some of them run. Morley had Martin come up, and I ran a portion of the blood samples so Martin could see how we were reading—how it was done—we ran just some of the worst re-actors. I made up my report on the condition of the dairy herd when I concluded my work on it. This is the original. I always make a copy and give it to the owner. I gave Mr. Martin a copy of the original report. He was present when I ran some [120] of them through. Contagious abortion is Bang's disease. Bang is the name of the professor that found the bug years ago. It is hard to explain that it is a disease. It isn't unique in cattle, swine may get it, and people and horses. The greatest ravages occur in dairy herds of the country. It causes great loss—it may cause a cow to drop her calf before maturity and others carry them till maturity or she herself may be a carrier of the disease or may become infertile and barren and may never have calves. The loss is terrific to the

(Testimony of Earl Francis Graves.)

dairy man. During part of its lifetime it lies quiet—remains dormant and then when in heat, when the sexual organs are active it may be more or less acute, as it were. Males can get it and often do. If it affects the testicles they are worthless and when they breed they just pump the germs into the cows. It might not be in the testicles and might be in other tissues and would not be so effective. The principal way of spreading the disease is from the mouth—drippings in pastures—the principal way of spreading is from ingestion. The cattle are not violently ill, the average animal may be a virus re-actor clinically, she may look all right but she may be barren or spreading the disease. Taking it by and large it would make the production of milk drop. Some animals would milk normally—the average animal they go way down. They do not necessarily dry up quickly. If they don't carry their calf to maturity they may never come fresh, as it were. If they drop a calf it is more likely than not that the milk would stop shortly. If they didn't carry the calf the full time there is a likelihood she might not give much or any, she might dry up. The cow is a dead loss to the owner, it is good only for slaughter. I think it would be entirely fair to say that cows affected with Bang's disease their value is simply their meat value, that is the instructions of the Government. In April, 1941 I definitely told Mr. Martin his cows could not be sold as milk cows but they could [121] be sold for slaughter. That was in April, 1941. I made a later examination of that

(Testimony of Earl Francis Graves.)

same herd on January 18, 1942, after Mr. Sheely was operating the dairy. The results showed 32 re-actors and 4 suspects, 8 clean ones and the others showed a slight degree of infection—a slight degree of reaction on tests. Of the 56 only 8 were clean ones—the balance showed slight reaction. In slight reaction — had they been entirely clean there shouldn't have been anything at all. I gave Mr. Shealy a copy of my original report. I told him the cows were quarantined to the place and could not be sold as milk cows. He could not take them to Palmer and put them on his ranch there. I don't have those records with me as to that herd, the Sheely herd at Palmer. I examined them last year. There were some re-actors at Palmer. I do not remember when the date was. I don't have the records and I would hesitate to guess as to whether that was after some of the Martin herd had been taken to Palmer or before. It would take me as long as it would take to go to Palmer and return to get the records.

Cross Examination

Upon cross examination the witness testified as follows:

Not to my knowledge is there any provision against selling milk from this herd. It would rest with the City ordinances, I presume. I can't say whether my office permits selling the milk as long as it is pasturized. My department has nothing to do with that. It could be sold if the City ordinances would permit. My quarantine was a quarantine

(Testimony of Earl Francis Graves.)

against transporting the cows. They had to stay there. It was not to destroy them. That is right, it was a restriction against moving them from the farm. I couldn't say what is the average production of cows as to milk. My only experience is as a veterinarian. I haven't had occasion to determine the normal milk production of cows. It varies so greatly —from nothing to many pounds per day. I [122] have no idea what the average would be. I have examined cattle in the Palmer area.

Q. Is there Bang's disease there?

A. Yes, sir, there is.

Grigsby: Objected to.

Court: It may be stricken.

The general husbandry was an improvement in the condition of the herd over the last time I examined the herd at the Step and a Half ranch.

Q. Did you make a statement in the presence of Mrs. Bass the condition of the herd was better?

A. It couldn't have been with the figures showing what they are.

I might have made that statement of the general welfare and husbandry but certainly not with reference to Bang's disease. I designate cows at the time of examination by putting tags on their ears. They generally stay on from one season to another. Some night get pulled out. Some of these were the same cows I examined the first time. I don't know whether other cows were there. We would have to compare this. I can state from my records which were the same cattle. It would take quite a little while.

(Testimony of Earl Francis Graves.)

Grigsby: Plaintiff desires to move to dismiss the second cause of action relating to the Palmer herd of plaintiff's without prejudice.

Court: A non suit without prejudice is granted.

Donohoe: I would like to find out what they are suing for.

I determined that 41 cattle were in the January test that were in the April 22nd test. 54 were examined in the April test.

Q. Fifty-four and bulls?

A. At least one was bull, I don't have them designated as to sex. I believe he had two.

I have been engaged in my present profession since 1927. [123] The Territory of Alaska is now my employer. Bang's disease is a prevalent disease. I don't know whether there is only one state in the United States that is free from it. It is difficult to keep up with it. Bang's disease is prevalent in the Territory of Alaska. I have had occasion to examine cows in other places in the Territory of Alaska and have also examined them for tuberculosis. I do not order the extermination of a Bang's diseased cow. It is stated in the law that there is a prohibition as to moving cows from the place where they are. I did not order that they be killed. I couldn't tell you what is the percentage of cows in a herd that are normally dry. I have no idea. No, I wouldn't say that assuming a herd of the size of this herd which had 58 cows in it at the time of the transfer from the Martins to Sheelys were producing milk in quantities of 210 to 215 gallons per day and selling

(Testimony of Earl Francis Graves.)

at an average price of 80 to 90c per gallon was of no value for any purpose besides meat.

Q. Did you testify this morning that this herd had no value because of Bang's disease—no value except for meat.

A. It may be a bit abstract—if you got only a pint of milk and there was sufficient market for it certainly that quantity of milk would have considerable value, but the potential loss is terrific in loss of calves and sterility of cattle and the chance or possibility of people becoming ill from using the milk, the general public would be much better off with the animals destroyed.

Q. Didn't you testify you didn't require them to destroy the animals?

A. There is no such provision.

Q. They can sell the milk if it is pasturized?

A. That depends on the the City Ordinance.

Q. As far as the Department goes that is true?

A. Yes.

Q. You have a policy over tuberculine cattle and order [124] them destroyed if diseased?

A. Yes.

Q. You do not do that with Bang's diseased cows? A. That is right.

Q. 210 to 215 gallons per day is that average or better than average? A. I do not know.

Q. Taking your qualifications of a moment ago as to the damage to the herd, you can't whether there was a substantial decrease in milk in this one's can you? A. That is true.

(Testimony of Earl Francis Graves.)

I am not sure that what I said is that as far as this particular herd is concerned it had no value except for meat purposes. The question would have to be read as to what I testified to this morning. Certainly this herd would have value for other purposes besides meat. Certainly it would have value as a herd producing milk. No, I don't know whether the production stated would be average or less than average or greater. I don't know what percentage were first producing. I don't know whether I discussed the matter with Martin. It would have no bearing on the subject so it is not likely. I don't know whether I discussed it with Mr. Martin.

Q. Didn't you tell Mr. Martin this was one of the best herds you had seen and it would be a shame to butcher it.

(The stenographic report of the record fails to show the answer.)

Upon

Redirect Examination

the witness testified as follows:

That is right. The records were made contemporaneously at the time of the tests.

Whereupon plaintiffs' Exhibit "A", being a report dated [125] April 22, 1941, and "B", being a report dated January 18, 1942 were received and marked, which said exhibits are as follows: [126]

April 22-1941

Plato
USDA BAI

— — — —
/ — — —
+ / — —
+ + / —
+ + + /

BANGS DISEASE TEST REPORT
Territory of Alaska

BF	29	54218	5		/	—	—	—		✓	29
BG	30	44756	6		+	+	+	+	✓	✓	30
BJ	31	58034	4		+	/	—	—	✓	✓	31
BH	32	60616	5		+	+	+	/	✓	✓	32
BG	33	7268	5		+	/	—	—	✓	✓	33
BA	34	95448	4		+	/	—	—	✓	✓	34
BA	35	91534	5		+	/	—	—	✓	✓	35
BI	36	98198	5		—	—	—	—		✓	36
BG	37	20643	3		—	—	—	—		✓	37
BI	38	9973	3		+	/	—	—	✓	✓	38

[Pencil Note]: A. T. Martin 1941

Identification Pltfs' Exhibit A. Sheely et al, Plaintiff, vs. Martin et al, Defendant.

No. A-2827 [128]

April 22-1941

BANGS DISEASE TEST REPORT
Territory of Alaska

Plate USDA BAI

Kind of Antigen _____

Serial Number 1388

Owner's Name A.T. Martin Address Anchorage, Alaska

"I certify that I have drawn these blood samples and correctly identified each eartag number or registration name or number. This is test of all dairy stock six months of age or over."

Signed Earl F. Reaves D.V.M.
Approval Veterinarian

21 reactors & Suspects

Eartag or Registration No.	Age	Sex	1/50	1/100	1/200	1/400	Remarks	Eartag or Registration No.	Age	Sex	1/50	1/100	1/200	1/400	Remarks
BI 256531	5		+	+	+	I	✓ ✓ 39	BH 24004	5		—	—	—	—	✓
BE 18237	6		+	+	I	—	✓ ✓ 40	2 BF 83602	5		—	—	—	—	✓
BI 42313	5	✓	—	—	—	—	✓ 41	3 BH 60046	5		—	—	—	—	✓
BF 150844	5		—	—	—	—	✓ 42	4 BI 9970	3		—	—	—	—	✓
BH 11473	6		—	—	—	—	✓ 43	5 BF 71779	6		+	+	+	+	✓ ✓
BE 56250	5		—	—	—	—	✓ 44	6 BI 9978	6		+	+	I	I	✓ ✓
BB 70858	6		I	I	—	—	✓ ✓ 45	7 BH 72859	3		—	—	—	—	✓ ✓
BB 92741	5		—	—	—	—	✓ 46	8 BB 59103	5		+	+	+	+	✓ ✓
BB 91342	5		—	—	—	—	✓ 47	9 BB 72247	6		+	+	+	+	✓ ✓
BB 43516	5		—	—	—	—	✓ 48	10 BI 57823	2		—	—	—	—	✓
BH 77940	5		+	+	I	—	✓ ✓ 49	11 BH 48481			—	—	—	—	✓
BE 2 6869	6		+	+	+	I	✓ ✓ 50	12 BH 66614			+	+	I	—	✓
BB 91636	6		—	—	—	—	✓ 51	13 BE 92044			+	I	—	—	✓
Alaska 14 615	5		+	+	+	+	✓ ✓ 52	14 BO 27506			—	—	—	—	✓ (22)
DC 15 56655	5		+	+	+	+	✓ ✓ 53	15 BH 47689			—	—	—	—	✓
BO 16 30717	6		+	+	+	+	✓ ✓ 54	16 BE 18237			+	+	+	+	✓ ✓
BF 17 74921	5		+	+	+	+	✓ ✓	17							
BE 18 73881	5		+	+	+	+	✓ ✓	18							
BE 19 43074	5	✓	+	+	I	I	✓ ✓	19							
BI 20 98154	4		+	+	+	+	✓ ✓	20							
BA 21 74989	5		+	I	—	—	✓ ✓	21							
BH 22 59953	5		+	I	—	—	✓ ✓	22							
BH 23 19690	5		+	+	+	+	✓ ✓	23							
Dupree 24 407	6		+	+	+	+	✓ ✓	24							
BM 25 95446	6		—	—	—	—	✓	25							
BE 26 73702	5		—	—	—	—	✓	26							
BH 27 65473	4		—	—	—	—	✓	27							
BI 28 58361	4		—	—	—	—	✓	28							
BF 58218	5		I	—	—	—	✓	29							
BE 30 44756	6		+	+	+	+	✓ ✓	30							
BI 31 58034	4		+	I	—	—	✓ ✓	31							
BH 32 40616	5		+	+	+	I	✓ ✓	32							
BG 33 7268	5		+	I	—	—	✓ ✓	33							
BH 34 44345	4		+	I	—	—	✓ ✓	34							
BH 35 91534	5		+	I	—	—	✓ ✓	35							
BI 36 98198	5		—	—			✓	36							
BE 37 20643	3		—				✓	37							
BI 38 9993	8		I	I	—	—	✓ ✓	38							

[Penciled No. 104] A. T. Martin 1941
Identification Plaintiff's Exhibit A. Sheely et al,
Plaintiffs, vs. Martin et al, Defendant.
No. A-2827 [128]

104

27

January - 18 - 1942

BANGS DISEASE TEST REPORT
Territory of Alaska

Plate
Kind of Antigen USDA-BAI.

Serial Number 1388

Owner's Name Mr. Ross Sheely Address Anchorage, Alaska

"I certify that I have drawn these blood samples and correctly identified each eartag number or registration name or number. This is test of all dairy stock six months of age or over."

Signed Carl F. Graves D.V.M.
Approval Veterinarian

32 Reactors
9 Clears
4 Suspects Other show slight

Eartag or Registration No.	Age	Sex	1/50	1/100	1/200	1/400	Remarks	Eartag or Registration No.	Age	Sex	1/50	1/100	1/200	1/400	Remarks
BI 1 56531	1	♂	+	+	+	+	39 Alaska	1 140		♀	+	+	+	+	
BO 2 42972		♀	+	+	+	−	40 BI	2 9970		♀	+	+	−	−	
BO 3 43074		♀	+	+	−	−	41 BI	3 9978		♀	+	+	+	+	
BH 4 77940		♀	+	+	+	+	42 BF	4 54215		♀	+	−	−	−	
BN 5 11422		♀	+	−	−	−	43 BO	5 44756		♀	+	+	+	+	
Be 6 56270		♀	−	−	−	−	44	6 218		♀	−	−	−	−	
BH 7 66614		♀	+	−	−	−	45	7 211		♀	−	−	−	−	
BH 8 92741		♀	+	+	+	+	46 BG	8 56455		♀	+	+	+	+	
BF 9 91342		♀	+	+	+	−	47 BA	9 91534		♀	+	+	+	−	
BF 10 56054		♀	+	−	−	−	48 BG	10 42312		♀	+	+	+	+	
11 201		♀	+	+	+	−	49 Alaska	11 1029		♀	−	−	−	−	
12 215		♀	+	+	+	−	50 BN	12 60046		♀	+	+	+	+	
BG 13 91636		♀	+	−	−	−	51	13 113968		♀	+	+	+	+	
Alaska 14 145		♀	+	+	+	−	52 BG	14 7268		♀	+	−	−	−	
BF 15 83542		♀	+	+	+	+	53 BI	15 71779		♀	+	+	+	+	
BH 16 41986		♀	+	+	+	−	54 BH	16 66473		♀	+	+	+	+	
BH 17 95446		♀	−	−	−	−	55 Ba	17 59103		♀	+	+	+	+	
BG 18 206443		♀	+	+	+	+	56 BI	18 57523		M	+	+	−	−	
Bj 19 55361		♀	−	−	−	−		19							
BA 20 74989		♀	+	−	−	−		20							
BA 21 59953		♀	+	+	−	−		21							
BA 22 21604		♀	+	+	+	−		22							
Alaska 23 145		♀	−	−	−	−		23							
BG 24 34090		♀	−	−	−	−		24							
Bh 25 41985		♀	+	−	−	−		25							
Ba 26 19690		♀	+	+	+	+		26							
Bh 27 49611		♀	+	+	+	+		27							
Bh 28 42679		♀	+	+	−	+		28							
Bo 29 6564		♀	+	+	+	−		29							
Bh 30 60610		♀	+	+	+	−		30							
Alaska 31 156		♀	+	−	−	−		31							
Bh 32 95449		♀	+	−				32							
Bi 33 97198		♀	+	+	+	+		33							
BO 34 37506		♀	+	−				34							
Bo 35 42536		♀	+					35							
Bj 36 9		♀	+	+	−	+		36							
Be 37 [illegible]		♀	+	+				37							
BF 38 [illegible]		♀	−	+	+			38							

[Pencil Note]: Ross Sheeley 1942.
Identification—Pltfs' Exhibit B. Sheely et al,
Plaintiff vs. Martin et al, Defendant.
No. A-2827 [130]

129

(Testimony of Earl Francis Graves.)

Whereupon Exhibit "A" was read to the jury.

As an interpretation of the plus mark and the minus mark where a minus is means negative, no reaction, the pluses mean positives, "I" means incomplete, not a definite reaction but there is something there. Yes, sir. A plus indicates the animal had Bang's disease. I can identify the paper you hand me. It is a Bang's disease report test on Ross Sheely's herd at Palmer, Alaska, dated March 7, 1941.

Court: Is that part of your main case?

Argument followed.

Donohoe: When was this report written out?

A. Whatever the date is.

Q. Is this part of your original records?

A. That is a copy of my original.

Q. When was the copy made?

A. On that date, this is a duplicate of my original.

Donohoe: Object to the offer, it is too remote and not pertaining to the issues in this case.

Court: Objection overruled. Exception allowed.

The offer was received and marked plaintiffs' Exhibit "C", being a report dated March 7, 1941, reading as follows:

March 7, 1921

Plaintiff's Exhibit C

BANGS DISEASE TEST REPORT
Territory of Alaska

29	"	150	2	F	"	29			
30	"	151	4	F	"	30			
31	"	152	1	F	"	31			
32	"	153	4	F	"	32			
33	"	154	1	F	"	33			
34	"	155	1/2	F	"	34			
35	"	56	1	F	"	35			
36						36			
37						37			

Identification—Pltfs. Exhibit C. Sheely et al, Plaintiff, vs. Martin et al, Defendant. No. A-2728.

[133]

132

March 7, 1921

BANGS DISEASE TEST REPORT
Territory of Alaska

Kind of Antigen Blue Label

Serial Number 1077

Owner's Name Case Sheely Address Teller, Alaska

"I certify that I have drawn these blood samples and correctly identified each eartag number or registration name or number. This is test of all dairy stock six months of age or over."

Signed Case & Graves Dunn D.V.M.
Approved Veterinarian

Eartag or Registration no.	Age	Sex	Reaction to Bangs Disease Test	Eartag or Registration No.	Age	Sex	Reaction to Bangs Disease Test
1 Alaska 127	4	F	negative	1			
2 " 128	4	F	"	2			
3 " 129	3	F	"	3			
4 " 130	3	F	"	4			
5 " 131	3	F	"	5			
6 " 132	3	F	"	6			
7 " 133	3	F	Suspect	7			
8 " 134	4	F	negative	8			
9 MV 5644 478	3	F	"	9			
10 " " 1 [illegible]	4	F	"	10			
11 Alaska 135	3	F	"	11			
12 " 136	3	F	"	12			
13 [illegible] 139	4	F	Negative	13			
14 " 137	2	F	"	14			
15 " 138	2	F	"	15			
16 " 139	2	F	"	16			
17 " 3 [illegible] 74	4	F	"	17			
18 Alaska 141	4	F	"	18			
19 " 141	2	F	"	19			
20 " 142	5	F	"	20			
21 [illegible] 5313	5	F	"	21			
22 Alaska 143	2	M	"	22			
23 " 144	1	F	"	23			
24 " 145	4	F	"	24			
25 " 146	1	F	"	25			
26 " 147	1	F	"	26			
27 " 148	1	F	"	27			
28 " 149	2	F	"	28			
29 " 150	3	F	"	29			
30 " 151	4	F	"	30			
31 " 152	4	F	"	31			
32 " 153	4	F	"	32			
33 " 154	1	F	"	33			
34 " 155	2	F	"	34			
35 " 156	2	F	"	35			
36				36			
37				37			

Identification—Plffs. Exhibit C. Sheely et al, Plaintiff, vs. Martin et al, Defendant. No. A-2728.
[133]

(Testimony of Earl Francis Graves.)

On that date, March 7, 1941, there were no reactors but there was one suspect in the Palmer herd of Mr. Ross Sheely affected with Bang's disease. There were 35 head of cows there.

The reading of plaintiffs' Exhibit "C" was waived.

There has not been found any cure for Bang's disease. In reference to Mr. Donohoe's question as to the value of a herd of cows that has Bang's disease and as to whether or not its value was more than its meat value, it might be, but he certainly wouldn't purchase such an animal as a dairy cow, I think it would be folly. The sale of such cows is prohibited.

Upon

Recross Examination

the witness testified as follows:

Q. The sale or the removal?

A. The law says the sale is prohibited.

Q. The law says you should kill them?

A. No.

Q. It says to own them is prohibited.

A. Yes, sir.

The type of report Exhibit "C" is a different type from Exhibits "A" and "B". "C" does not attempt to show the same information as given on "A" and "B". This is more for the layman, this shows a little more of the facts. Here I wrote the word negative. On Exhibits "A" and "B" there would have to be a plus after the animal to show

(Testimony of Earl Francis Graves.)

it had Bang's disease. Yes, there would have to be at least a plus, an incomplete would never get a plus.

Q. Does the one on Mr. Sheeley's herd you have marked as a suspect, would that have a plus after it.

A. My original would have, but ordinarily a layman doesn't understand a plus or a minus so I write it out.

Q. Then a plus after a cow on Exhibits "A" or "B" doesn't mean they had Bang's disease? [134]

A. Oh, yes.

Q. If they were suspects they would have that?

A. You can't split hairs, that is the designation as made by the Government.

Q. In Martin's plus means that Martin's had Bang's disease but on "C" it doesn't?

A. A suspected animal would.

Q. Are you sure that paper is the same as you prepared it on March 7, 1941, did you write that on there yourself?

A. No, that has been put on later.

Donohoe: We move to strike.

Court: I think the writing on the side should be stricken from that exhibit.

Donohoe: We move to strike the exhibit.

Court: The writing may be taken off.

Donohoe: Exception.

Court: Exception allowed.

The incubation period for Bang's disease is from a very few days to 30 or 31 days. I mean by a few, four or five. I said a moment ago that Bang's disease wasn't curable.

(Testimony of Earl Francis Graves.)

Donohoe: In order to keep the record straight we have to show what is on that exhibit.

Court: The record may show butchered was written on in two places after the report was made. The Court ruled that they may be stricken.

Donohoe: Exception. The exhibit is not as originally prepared and will have undue influence upon the jury in the trial of this case.

Court: No objection was made at the time the exhibits was offered on account of those words being there. Exception allowed.

I think the date of the third exhibit is March 7. As to whether or not those were Sheely's cows I examined that day or [135] other cows from other parts of the valley, I examined them at Sheely's ranch, I presume that Mr. Sheely owned them.

LLOYD A. MORLEY

was called as a witness on behalf of the plaintiffs and being first duly sworn, testified as follows:

My name is Lloyd A. Morley. I live at Anchorage and am senior sanitarian with the Territorial Department of Health. My employment is under the Territory of Alaska, under the Territorial Commissioner of Health's office. I helped in taking the blood samples to assist Dr. Graves in the examination of the cows of the Martin ranch in April, 1941. I held the cows and numbered the samples for Dr. Graves. I then brought the blood samples

(Testimony of Lloyd A. Morley.)

back into town. As far as I know Dr. Graves examined them in the hotel room. Some were run in the Territorial Department's branch laboratory. That is my office. Myself and Dr. Graves were present and I phoned Mr. Martin. A routine report was made by Dr. Graves as to the result of that run. We received the same report in our office which you received as Exhibit "A"—we do not have Exhibit "B". Mr. Martin was present when part were run. I took Dr. Graves out in my car and he delivered a copy to Mr. Martin.

There was no cross examination.

ROSS L. SHEELY

one of the plaintiffs, being first duly sworn, testified as follows:

My name is Ross L. Sheely and I live just outside of Anchorage. I have lived in Alaska about 12 or 13 years. Prior to moving just outside of Anchorage I lived at Palmer where I was a farmer. My farming included production of hogs, dairy supplies, dairy products, eggs, grain and hay. I had a dairy at Palmer. We milked some cows.

It was thereupon stipulated that the exhibits attached to the complaint, counter-claim and reply are identical and do not have to be re-introduced and can be referred to as Exhibits "A", [136] "B", "C" and "D". The reading of the exhibits was waived.

(Testimony of Ross L. Sheely.)

I entered into an oral agreement with the defendants for the purchase of the Martin dairy in June, 1941.

Q. I notice in Exhibits "A", "B" and "C" that your name is not on the list, not a signature to it but as a guaranty, will you explain to the jury how that situation arose?

Donohoe: Objected to as incompetent, the pleadings and exhibits speak for themselves.

Court: Objection overruled. Exception granted.

A. At the time of this deal when this contract and papers were signed, myself and my family, Jack and Joe and Mrs. Sheely were operating as co-partners as a family. I was under contract, farming under the Co-Operative Association who had done no business out of the valley and it would be impractical and impossible to produce milk here, haul it to Palmer, pas*tue*rize it and haul it here for distribution. I couldn't do that nor could they do it, they don't pick up milk. In order that my product here could not conflict with the product from the valley farm on which membership in the Co-Op was based I didn't want my name to appear on this contract here not knowing the reaction of the manager of the Co-Op to producing a product away from the valley. It would have been suicide to produce it here and haul it to Anchorage. I would look like a competitor. That condition might have arisen—in order to eliminate that, as the rest of the family were not on contract there they signed the contract and all products of the farm at Palmer were sold

(Testimony of Ross L. Sheely.)

through the Co-Op and would be as long as I remained a member. The Board of Directors later thought it better that I discontinue my membership in the Association, which I did.

Q. On whose behalf were these contracts or guaranty?

A. I did that at the demand of Mr. and Mrs. Martin. After making the deal they refused to accept the signatures of the other [137] three unless I guaranteed fulfillment.

$9800 was paid on the conditional sales contract on July 28, $1541.10 was paid between then and the first of January, plus $450 interest. The conditional sales contract covers the sale of the cattle—56 cows and one bull.

Q. In arriving at this purchase price how were the cattle figured? A. At their cost.

Donohoe: Objected to as incompetent, irrelevant and immaterial. The contract is in evidence and sets up the purchase price.

Court: Objection sustained.

A. $300 apiece.

Q. $300 a head? A. Yes, sir.

I took possession of the cattle the first day of July, 1941. I am still in possession of the farm.

Q. How much milk were the cows giving at the time you took possession?

Court: It is immaterial.

My first definite information that this herd had Bang's disease came when I was told that it would not be permissible for me to take these cattle from

(Testimony of Ross L. Sheely.)

Anchorage farm when they dried up to Palmer where I could operate at much less cost as I had a stubble field, etc. When told by the veterinarian I was liable to the law and would be prosecuted. Prior to that I had been taking them to the Palmer ranch. I was told this practice must stop in October or possibly November, 1941. The cattle aborted. August 26th, 1941 is the first abortion.. August 26th, 1941 is the first one I had after taking the place over. Sometimes cattle will abort a calf other than from disease. I thought from the size of the herd it might have bee*m* bumped or slipped [138] and I did not suspect on that date that the whole herd was infected. On September 6, 1941 two cows aborted, the 6th of September. The next cow was September 18. The next cow October 7. The next cow November 5. Then November 8, November 12, December 8. The cows that reacted definitely, with two exceptions, those cows did not come to a very high milk production. One came up to about as much milk as it would have normally given. The others hardly gave enough to pay to milk them. In a few cases cows which aborted, in many cases were giving milk at the time and continued about as they had after they got over the sickness of the abortion continued as they had before. They dropped down in their milk supply. Instead of being fresh cows, they were milking as cows fresh 9 or 10 months previously. I would say aborted cows gave 50% of normal production. When these cattle aborted the milk supply gradually dried up for a period. In the

(Testimony of Ross L. Sheely.)

average case they would not breed again. They will, after aborting, cows frequently go for several months before they will accept the service of a bull, they often become sterile and there is a long period of months in the majority of cases before they can get pregnant again. They were confined to the ranch where feed is high priced so I butchered them. I have butchered about 35 or 36 head. Of the original Martin herd those that are left won't vary more than one or two—there are 16 or 17 head. I certainly did not know at the time of the purchase that the herd was afflicted with Bang's disease.

Q. Now to go back a moment, you paid $9800 on the purchase of the cattle, paid that at the time of the execution of the instrument?

Donohoe: That is not a fair question—it is on the whole thing, not on the cows.

Q. The monthly payments were $308—you testified how much you paid on the conditional sales contract? [139] A. That's right.

I paid $110 on the grazing permit. I paid $200 a month on the lease for the ground. That is Exhibit "A". $1200 I believe was paid on that lease. At the time I purchased the place Mr. Martin had a truck on order and the old truck was valued and turned in on the new truck at $550. I have completed the payments on that. As to how much I paid for the hay and grain that was on the place I couldn't segregate what was on the place—there was a carload of hay and a carload of grain ordered

(Testimony of Ross L. Sheely.)

when I made the agreement. I believe they came in about the time of the written contract. I was to pay for what was on order, it was around $2000. I have added additional equipment to the dairy and made extra expenditures on improvements on the dairy. For equipment, supplies and improvements $2513.15. I have it itemized — milk cases, quart bottles, foot bags, half pint bottles, pump for milking machine, cartage on hay and grain, box stall, closets in house, manuring, pasture, clearing land, paid on separator motor, painting milk room, wiring on separator, lumber for floor in feedway of barn, another motor, filter and blackout equipment on the barn. What I paid on that new truck is in the $2500. It was put in at the time this was made up in December. As to how many of the original Martin herd I have on the premises at the present time my answer before was not exact. I think I said within 2 of right—that is 16, in a minute I can tell you exactly. I have exactly 14 head of cows on the place which were in the original Martin herd and one below. I have 27 cows on the place now. I think the way it would come out is the difference between 14 and 27 or 13 is the number that I have brought down from the Palmer place. I cannot move those 13 off the place. I think it is exactly 36 cattle that I have killed. Those all belonged to the Martin herd. I believe 6 or 7 of the diseased cattle have died. I received $4472.20 for the cattle that were [140] slaughtered.

(Testimony of Ross L. Sheely.)

Upon

Cross Examination

the witness testified as follows:

My occupation before I commenced dairying in Palmer was I farmed at Palmer. Before I got any cows I raised chickens and pigs. Before that I was manager of the Corporation. Before that my occupation was with the Extension Service. I was not teaching agriculture. I will qualify that in this way. The Extension Service is supposed to carry the results of experiment stations to the public in general. No I was not carrying on experiments with cows in the Extension Service. No, the Extension Service didn't have anything to do with dairying. As to whether they had anything to do with that in experiment stations, when they carried on experiments and a bulletin was published it became the duty of the Extension Service to distribute that information. As to whether or not it was primarily my duty to distribute that to farmers, it was on phases of agriculture and home economics. When I was manager of the Corporation it was largely construction, land clearing and the building of houses and barns. Since I have been running the farm at Palmer I have been at times taking care of cows belonging to others. Yes, in the Summer of 1941 we took in some cows that were not our own. We had some cattle there in the Spring. I don't know the dates, I had some from two different people, Walter E. Huntley and Neil Miller. I had some on the place in the winter of 1938 from the Corporation and none after

(Testimony of Ross L. Sheely.)

that. As to cows that were taken back under conditional sales I have not had any since then. I had the Huntley cows the middle of the winter of 1940 and 1941. They stayed there until June, 1941. I got Mr. Miller's cows possibly in March, 1941. I believe there were four. There were two of Huntley's. As to the dates when I butchered the cows previously [141] mentioned they were April, the 19th of October, 1941; Belle, the 3rd of March, 1942; Bertha, the 10th of February, 1942; August 7, 1941; October 12, 1941; October 25, 1942; October 12, 1941. October 12, 1941 there were two on that date, that sometimes occurred. October 20, 1942; October 15, 1942; October 21, 1942; November 7, 1942; November 5, 1942; October 3, 1942; October 14, 1942; January 25, 1942; August 7, 1942; January 31, 1942; October 6, 1941; November 11, 1942; September 14, 1941; September 2, 1942; December 14, 1941; October 29, 1942; October 20, 1941; July 1941; I don't have the date in there. I possibly have it in the other book. That was a cow that was taken to Palmer; as soon as we found she was a re-actor we butchered her there—a cow from the Martin herd. November 12, 1942; November 2, 1942; May 22, 1942; October 12, 1942; September 8, 1942; September 2, 1942; November 16, 1942; September 3, 1942; November 14, 1942. The last cow I butchered I haven't posted in this book. I have it at home. That was in November of this year. The last cow butchered was March 22, 1942. That is the last one in my book but it is alphabetical. Yes, I think I

(Testimony of Ross L. Sheely.)

have named now all the cows I have butchered. That is only from the Martin herd. I did not include anything of my own. I have butchered six others that I haven't included here. The amount I have been getting for beef in November of this year varied, depending on the cow. The average for beef now has been 28c, commencing lately. It used to be 18. Yes, 28c this fall. I think from the middle of September was the last time they would do any good grazing in the open this year but I kept them outside for exercise after that.

Q. Mr. Sheely, in addition to these and those you testified aborted, you butchered 36 calves and sent six to Palmer didn't you? Of the total calves 36 were butchered, 6 were sent to Palmer and 6 died?

A. I never made a statement of the calves. [142]

Q. You mean there were no live births?

A. Aborted calves are sometimes alive and sometimes dead.

Q. Out of the births—either aborted or otherwise—36 were butchered, 6 sent to Palmer and 6 died, is that correct? A. I don't know.

Q. Look at that book and look at the references to births and answer that?

A. When this book was handed to you it was folded right here showing the cattle, it was turned over another sheet, there is a compilation here 12/21/42, it says 36 butchered, 6 died, 6 sent to Palmer, that has nothing to do with what I testified to.

(Testimony of Ross L. Sheely.)

Q. Answer the question please?

A. I don't know.

Q. You can refer to that record and find out?

A. Yes, sir.

Q. Will you do it then?

A. As far as I can compute this Mr. Donohoe, there is 8 calves died, no 16 died, 13 went to Palmer, killed 18 and gave 8 away, I may be wrong on the number killed.

Q. As a matter of fact you took approximately 35 to Palmer but there might be some you gave away, were some included in that? A. Yes.

Q. Didn't you take 35 calves to Palmer?

A. No, around 20.

These calves were not vaccinated when they were born. I sold meat to different people in town. I have no contracts with people to sell meat. Part of the meat went to the hospital, not on a regular basis of delivery. Sometimes they buy a cow from me and sometimes from somebody else. I have not made any payments on the lease since December. I still have possession of the personal property leased other than the cows. I did not sell the cat. I didn't let anyone else have it. No, sir, I didn't rent it. [143] Mr. Bailey used it some. Yes, sir, for moving houses in town. As to whether I got anything out of it, I had the use of his tractor in Palmer. Rather than take this cat to Palmer we traded. No, I don't believe I have traded any other property other than cows. No, sir.

(Testimony of Ross L. Sheely.)

Q. How much have you received from the butchered calves?

Grigsby: Objected to as immaterial.

Court: I will not go into the increase. Exception allowed.

Q. How much have you received from the sale of milk from these cows.

Grigsby: Objected to.

Court: Objection sustained. Exception granted.

I don't believe I have rented anything else from that farm to anyone that I bought from Mr. Martin. I still have possession of all the rest other than the cows. I got only one bull and he is still there. I paid Mr. Martin on the truck that I got, $550 the value of the old truck. The balance I paid to Well's Motor Company. Since then I have sold that truck myself. I included part of the payments that I made on the truck in the statement. I paid Mr. Martin for hay and grain and not to hay and feed companies that shipped it. I don't believe there was any hay or grain inventory to me. If there were any on the farm, if there was a few bags there I paid for them. The itemized list Mr. Martin gave me would show that. I paid for the new shipment. It is correct that this hay, grain and feed I received and paid for was a new inventory coming in and was used to feed the cows afterwards. I butchered the animal shown on plaintiffs' Exhibit "C" as a suspect. It was butchered as soon as I could get to the slaughter house to butcher it.

(Testimony of Ross L. Sheely.)

Court: You say you have 13 cows you brought from Palmer you can't take off? A. Yes, sir.

[144]

Q. What is the calue of those cows?

A. $3900, as dairy cows.

Q. You value them at $300 apiece.

A. Yes, sir.

Q. You agreed to pay $200 a month for the rental of the land for a going dairy? As it was at that time? A. Yes, sir.

Q. What is the reasonable value of rental considering this herd was infected?

A. Well, I thought at the time I bought it it was satisfactory.

Q. What was the reasonable value of the rental as you occupied that place?

A. Perhaps $50 a month.

Q. You think that $50 a month would be reasonable? A. Yes, sir.

Q. You say you made improvements in the sum of $2513.15, how much of that is for permanent improvements, less the money you paid for the truck and for supplies.

A. Milk cases are permanent and milk bottles are subject to inventory.

Q. You have a motor—that would last for 50 years?

A. No, they don't last that long because it is wet in the milk room, they don't last over two or three years.

(Testimony of Ross L. Sheely.)

Q. Will you look that over and see how much is permanent and how much is for repairs and replacements?

A. May I say this was made last December.

Q. I think it should be brought up to date.

Donohoe: I couldn't very well object to the questions of the Court, but if your Honor please I move to strike the answers of the witness as incompetent, irrelevant and immaterial.

Court: Motion denied. [145]

Donohoe: I also object to the testimony of this witness as to monies spent by this witness as incompetent. This witness was not a party to this contract.

Court: Was this money paid under the contract?

A. Yes, sir.

Q. And you know it was paid under the contract?

A. Yes, sir.

Court: Motion overruled. Exception allowed.

Donohoe: He testified he paid it.

Grigsby: On whose behalf was this money paid —on your part or on the part of the co-partnership?

Donohoe: Object, there is no mention of a co-partnership in the agreement.

Court: You may have an exception.

Court: I asked you what part of the $2513.15 is for permanent improvements and what for repairs? A. I have such statement.

Q. How much is for permanent improvements?

A. $2020.

Q. And the rest is for repairs?

(Testimony of Ross L. Sheely.)

A. Yes, I brought it up to date, with feed and supplies included.

Donohoe: If the Court please, defendants at this time move the answers of the witness be stricken as incompetent then, that is not at the commencement of this action.

Court: Motion denied. Exception granted.

The paper was thereupon offered, received without objection and marked plaintiffs' Exhibit "D", as follows:

ITEMIZATION OF EXPENDITURES AND PERMANENT IMPROVEMENTS AND SUPPLIES

June 28, 1941	Supplies, milk cases, etc.	$ 32.50
June 28, 1941	Quart Bottles	110.90
June 28, 1941	½ Pint Bottles	80.00

[146]

June 28, 1941	Pulso-Pump (Purchased from Martins, still unused)	103.00
Finish Nov. 10, 1941	Heating Plant	721.70
Finish Nov. 10, 1941	New Hay Barn	300.00
Sept. 1941	Mangers in Cow Barn	110.00
Nov. 2, 1941	Box Stall	75.00
Oct. 20, 1941	Closets	75.00
Oct. 18, 1941	Clearing Land	45.00
July 1 to Oct. 31, 1941	Manuring Pasture	150.00
Nov. 1941	Milk Pump Motor	17.50
Nov. 15, 1941	Separator Motor	40.00
July 1941	Painting Milk Room	6.00
Oct. 1941	Wiring on Separator	1.90
Aug. 1941	Window Shades	13.40
Sept. 1941	Clothes Line	2.45
Aug. 1941	Lumber for floor in feedway of barn	32.50

(Testimony of Ross L. Sheely.)

March, 1941	Crepaco Electric Motor—Milk Pump	17.50
Sept. 1941	Towel Racks & Fixtures	11.75
Sept. 1941	Filter—line with fittings	43.55
Dec. 24, 1941	Barn Blackouts	40.00

Supplies on Order

Dec. 19, 1942	1 BBL Sterichlor	$ 28.00
Nov. 18, 1942	1 BBL Wyandott	27.00
Oct. 17, 1942	10,000 Buttermilk Caps	10.00
Oct. 1, 1942	10,000 Cream Caps	10.00
Hay Ord. Dec. 12, 1942	1 car ordered from Seattle either just leaving or soon to leave 1 car hay in Seward enroute (bill received)	428.70

Supplies on Hand (Dec. 22, 1942)

182 sacks mixed 21% Protin dairy feed	689.78
2 tons hay @ 40.00	80.00
80,000 caps @ 2/57 per M/$2.50 per case freight	256.60
1 2/5 carbon caps	27.10
1 Carton caps	19.10
1/2 BBL Sterichlor	14.00
1/2 Wyandott	13.50
2/3 BBL soap Powder	20.00
18 sacks Beet Pulp	82.98
Sawdust for bedding	25.00
Rental bottle capper	28.00
650 Gals. Diesel Oil ¼ 12.7	82.55
2 tons of Coal @ 15.00	30.00
Total	$3,901.96

Identification—Pltfs. Exhibit D—Sheely et al, Plaintiff, vs. Martin et al, Defendant. No. A-2827.

Cross Examination continuing

Exhibit "D" covers the period of time from the time of the purchase of the place down to the present. The rest of the improvements were all made

(Testimony of Ross L. Sheely.)

prior to the commencing of this action. I am referring to improvements to the barn, the new hay barn. As [147] to whether I can mark opposite them the dates, they are all supported by vouchers I have in my files. I can approximate the dates within 30 days of any of them.

Court: I will permit the withdrawal of the exhibit so that you can put the dates on.

Yes, this includes such items as supplies on order and on hand. That would be difficult to date them.

Court: You can put the date of the order on if they haven't been received.

The following buildings are situated on the land covered by the lease: the house and barn, two barns, a storage shed and bunkhouse and garage. The house is probably an average of 50 by 20. That is the house where I am living now. I don't know how many acres of land there are. I would say approximately 8 or 10. 240 acres are included in the grazing permit less a small tract which has been withdrawn on which they are doing some air field work. We have had some difficulty, particularly the hay, in getting supplies to operate. During this past summer and fall we have not been having trouble getting help.

Q. Mr. Sheely, have you stopped making local deliveries in town except to wholesale accounts and the Army?

A. With the exception of two or three customers who are directly between the ranch and the down town district.

(Testimony of Ross L. Sheely.)

Q. Did you do so at the time I have mentioned do so due to a shortage of help?

A. There was a number of conditions. War conditions, automobile conditions, restriction of tires was perhaps the most important.

There was no discussion regarding Bang's disease with Mr. Martin at the ranch prior to purchasing it. I recall being present in your office together with my family, Mr. Martin, Mr. Cuddy and yourself, and discussing the clause in the contract of no [148] warranties and that there was a discussion regarding to my having inspected the cows, knowing their condition and that there was no guarantee on it. We were in your office. I was there and Mrs. Sheely, Jack, Joe, Mr. and Mrs. Martin, yourself and Mr. Cuddy. Mr. Cuddy said what about Bang's disease. Mr. Martin said I don't know anything about it, but he did know about it. He knew it was against the law to sell diseased cows. All he said was there was no warranty in the contract. He said there was no warranty as to the health of the cows. He did not tell me whether it was possible to determine whether they had Bang's disease. A very short time, was the period of negotiation for the purchase of these cows, not to exceed a week. As to whether I had the cows tested for Bang's disease, they weren't mine. I couldn't have them tested. No, it didn't occur to me to have them examined. I knew it was against the law to sell them. As far as possible I made an examination of them. There was no veterinarian available. Mr. Graves was not

(Testimony of Ross L. Sheely.)

available. I believe all that summer until way in August he was in Southeastern Alaska. No, I did not make any attempt to. It never entered my head that it was necessary to have a detailed examination. I didn't ask if they had tuberculosis. Those are things prohibited by law and it took me some time to find that out.

Q. How long have you been buying cattle, milk cows, for yourself or others?

A. The first bunch I bought to amount to anything was at Palmer.

Q. Have you bought any others?

A. One or two.

Q. Did you ever have them examined for disease.

A. No, sir.

Q. Never did. A. No, sir, not at my ranch.

[149]

Q. You knew that there was a City ordinance to pasteurize milk, local milk, because of Bang's disease in this locality? A. Many years ago?

Q. No, two years ago? A. No, I don't.

Q. Didn't you know all milk in this locality had to be pasteurized because of Bang's disease?

A. Had to be pasteurized?

Q. Because of Bang's disease?

A. I didn't know that, no, I wasn't living here then.

Q. You were living at Palmer? A. Lately.

Q. When do you mean? A. 1941, no 1940.

(Testimony of Ross L. Sheely.)

Q. Since then you have been selling milk?

A. To the Co-Op at Palmer.

And upon

Redirect Examination

the witness testified as follows:

I understood the question as to the value of the cows that I had put on the dairy here in Anchorage from the dairy at Palmer as to what they were worth when brought to the dairy as dairy cows, I said $300. Now they are worth what they are worth for meat. I can't move them. I can't take them off the place.

Recross Examination

(By Mr. Donohoe)

There are at this time 12 cows on the Step and a Half farm that were brought from Palmer, 18 cows and 1 bull were brought from Palmer. As to the dates when they were brought, I brought one cow in July, 1941. I question whether my records would tell you the approximate date. I don't have an individual record of my milking cows. No, sir, I don't keep a record of whether I milk the cows or not. we milk every day and night. No, in the [150] record where I have the names of the cows I don't have a record of where they were. I have it within thirty days. If I tell you how many were brought in July, is that satisfactory? Eight cows in July, 1941. There were four cows in September, 1941, one cow in August and I will say one in October. I am a little at loss to know when the bull was brought

(Testimony of Ross L. Sheely.)

in, I might be able to find that in some records I have at home. I brought the bull in May 19, 1942 and the last four cows were added to the herd on November 8, 1942. I don't believe I did bring down three or four cows when I brought the bull down on May 19, 1942. I believe it is correct that I brought down two cows when I brought the bull down on May 19, 1942. My other tabulation must be off two cows somewhere. The two cows were added in the count before which were taken back to Palmer which when tested did not have the disease. Two cows brought down here and milked and taken back to Palmer and tested and had not contracted the disease, they were not killed and are not here. No, these were not the two that were brought down with the bull, two other cows. I took them in the fall of 1941, or early in the winter. They were probably down here a month or so, two months at the outside, probably through July and August and early September. Three or four of the Martin herd were taken to Palmer, in the month of July, 1941, some of them, I don't believe I can tell you the number of cows specifically and the dates within a month. Five were taken up there in July and August, 1941. I couldn't say positively that I have not taken any cows to Palmer since July and August, 1941. Early in 1941 were the last cows taken to Palmer; none whatever to put in the herd up there. I haven't taken any cows to Palmer in 1942. I don't believe any whatever. No, sir, I can't recall a single one. No one else took any up for me. Some of these cows

(Testimony of Ross L. Sheely.)

were left at Palmer; two were brought back just before they freshened. Pretty and Pink were taken back here. Then two or [151] three of them were found to be re-actives and were butchered there. These two cows were brought back here early in September, 1941. I do not have any of the Sheely herd left in Palmer. No, none of the Martin herd, there wasn't a Martin cow left at Palmer prior to the fire, none at all. Yes, sir, I did have some of the Martin herd calves there.

CHARLOTTE SHEELY

one of the plaintiffs, being called as a witness, being first duly sworn, testified as follows:

My name is Charlotte Sheely. I did sign the contract which is a conditional sales agreement and lease.

Q. Covering the purchase of cattle on the Martin ranch and a lease of the property on behalf of whom were those three signatures?

Donohoe: Object as incompetent. The papers speak for themselves.

Court: She may testify. Exception allowed.

A. I signed it for the copartners, the four, Mr. Sheely, myself, Jack and Joe.

There was no cross examination.

JOHN H. SHEELY

one of the plaintiffs being called as a witness, being first duly sworn testified as follows:

My name is John H. Sheely and I am one of the plaintiffs in this action. I am not positive as to the date. It was in the latter part of June. I was a party to the agreement, being the conditional sales contract covering the purchase of cattle at the Martin ranch and lease of the property there.

Q. And in whose behalf did you sign such instrument?

Donohoe: Object to the question.

Court: Objection overruled.

Q. For whose benefit did you sign that agreement? [152]

Donohoe: Object as incompetent, the papers speak for themselves.

A. Well, I signed it on behalf of—we were planning a partnership, we were going to work it on shares.

Q. Who were the partners?

A. Mr. and Mrs. Sheely and my brother and myself.

Q. Where is your brother now?

A. En route from College, coming *hom* for the Christmas holidays.

ROSS L. SHEELY

being recalled, presented Exhibit "D" with the dates.

Upon

Cross Examination

(By Mr. Donohoe)

testified as follows:

I have prepared the dates on Exhibit "D". The heating plant, $721.70 was purchased new. As to whether or not these items were purchased new, some were on the place and I purchased them from Mr. Martin. It was in the contract that I would take them. They were not included in the purchase price. Some materials in the barn were brought down from Palmer. I valued that by taking the labor; I hired that done and so many thousand feet of lumber, part second hand and some new. I haven't anything on the item of valuation for the lumber. There is $33 for the barn. That is the cost price for second-hand lumber and the price of the new lumber, $25 per thousand for the second-hand lumber. I believe the labor amounted to $75. I gave a couple of boys a contract to build it for $75 who had done some work for me before. Yes, all the other items on the list were new, including the lumber used in the manger and the floor—there was no lumber in the manger.

Court: The cattle killed or butchered at Palmer, were they included in the first list you gave us. You testified there were [153] 36 slaughtered, the 3

(Testimony of Ross L. Sheely.)
taken to Palmer first are they included in that number? A. Yes, sir.

Donohoe: The defendants move for a non suit on the grounds that there is insufficient facts to state a cause of action.

Court: Motion denied. Exception allowed.

Donohoe: Defendants move for a non suit on the grounds that plaintiffs have not introduced sufficient evidence to sustain their complaint.

Court: Objection overruled. Exception allowed.

Whereupon the court announced he would hear from respective counsel as to the nature of the action.

JACOB BASS

was called as a witness on behalf of the defendants and being first duly sworn testified as follows:

My name is Jacob Bass. I was employed from June 28, 1941 until May, 1942 on the Step and a Half ranch. I worked for Mr. Martin for 13 months and Sheely 11. I didn't keep track of the date when I started working for Sheely. I worked for him during a period of time he operated the ranch. I left it May 19th of this year, 1942. Yes, I was on the ranch working for Mr. Sheely from June 28, 1941 to May 19, 1942. I was taking care of the cows. Yes, while employed there cattle of Mr. Sheely's were brought to that ranch from Palmer. I can't say when it was. I never saw good calves

(Testimony of Jacob Bass.)

come from his cows yet. The first cattle came after Mr. Sheely had it about a month. Yes, I know when some of the Martin herd were taken to Palmer, it was shortly after the Sheely cows were brought down from Palmer. I think there were 52 or 53 cattle on the Step and a Half Ranch when I left in May, 1942. The milk supply was a little better than 200 gallons when Mr. Sheely first took over the Step and a Half Ranch in June, 1941. When I left it was 85 to the milking—twice [154] a day. That would be 170 gallons a day. Yes, there was a change in the feeding of those cattle, in the hay. That was hay and alfalfa hay. There is much better milk in alfalfa hay. The hay came from Matanuska. No, this is not the same type of hay this herd was getting when it was producing 200 gallons a day. That was the feed from Mr. Martin.

ASA T. MARTIN

one of the defendants called as a witness on his own behalf, being first duly sworn, testified as follows:

My name is Asa T. Martin. I reside at 1108 Fourth Avenue, City of Anchorage. I am one of the defendants in this action. Sheely has paid me $9800 under the conditional sales agreement, Exhibit "A". That was the down payment made. He made monthly payments including December, 1941. No other payments were made after December, 1941. As to whether he made any payments to me

(Testimony of Asa T. Martin.)

for stock, he paid for the goods that were ordered as per agreement. They were coming in. Offhand I don't know the exact amount. I paid the bills and he reimbursed me. Yes, sir, I also paid $550 on a truck. Other than those payments no other sums were paid to me by Sheely under this contract. The lease Exhibit "B" was paid up to December, 1941 only. There have been no payments since then. One year was paid on Exhibit "C", $110 and nothing other than that. I did have a conversation with Mr. Sheely prior to his purchase of the place with reference to Bang's disease. I insisted on that being written into the contract, no warranty. Mr. Sheely asked me out behind the barn. I said I couldn't say the exact status. I said some was shown a year and a half ago and I had butchered some reactors since then and couldn't state the present status. I said I was going to vaccinate the cows in the future. He asked when we had had an abortion and I said quite a while ago and he said he considered that good. The milk production at the time of the sale was 200 gallons a day. [155] About one-sixth of the herd would normally be dry. As to the average production of milk of a herd, I will take the records of other people. I think the records will show three gallons is high, having a herd of 50 cows, that is above the average.

Upon

Cross Examination

the witness testified as follows:

This conversation with Mr. Sheely was previous

(Testimony of Asa T. Martin.)

to the time of the sale of the herd, when he was inspecting the place. It was only a few days before the purchase, a very few days before the purchase in which he talked about Bang's disease. I told him some were re-actors according to the veterinarian. Graves was the veterinarian. He didn't ask me to show it to him. Just he and I were there. No one else was there. No, he didn't ask me to tell him the gist of it. No, I didn't tell him I had the report. I had a copy. No, he didn't ask to see it. No, he didn't ask how many were infected or any details at all. Yes, I signed the answer in this case. Yes, that is my signature to the verification. Yes, sir, I think I read that over before I signed it. Well, I am not sure whether Mr. Donohoe was present or not when I read it over. Yes, sir, I read paragraph 8 of the answer before I signed the answer. Before I swore to the answer I read Mr. Sheely's complaint and that of the co-plaintiffs. I read all of it. Yes, sir, I read paragraph VIII. Well, as I interpret that paragraph, it specifically states that I was aware of the fact and Mr. Sheely was not aware of it. I can't see why Mr. Sheely wasn't—I told him all I had was the veterinarian's report. Mr. Sheely did ask me at the time I had the conversation about previous abortion of the herd. All I bought were tested before they left the states. I was adding to my herd right along. I did not bring those in to replace cows I slaughtered. I did butcher aborted cows. I think there were three young calves on my place when he took over. [156] There was one

(Testimony of Asa T. Martin.)
cow which had a sore foot which I gave to Sheely. Right. Mr. Sheely and I alone had the conversation in which I informed him about the herd having more or less Bang's disease. Yes, that is the only conversation I had with any of these co-partners about this.

Donohoe: Did you have another conversation in my office with Mr. Cuddy and Mr. Sheely?

Grigsby: Object he just testified it was the only one he had.

Defendants rest.

Argument.

Donohoe: They have to elect as to the cause of action, that is why I have been objecting throughout the trial.

Whereupon

ROSS L. SHEELY

one of the plaintiffs, was recalled in rebuttal and testified as follows:

I heard the testimony of Mr. Martin given in this court. No such conversation was entered into as testified by Mr. Martin at the barn on the Martin ranch in which the matter of Bang's disease in the cows was discussed.

Whereupon taking of testimony was closed.

Donohoe: I renew the motion for non suit upon the ground that the complaint does not state facts sufficient to state a cause of action.

Court: Objection overruled.

Donohoe: The same motion of not sufficient evidence to sustain the allegations of plaintiffs' complaint.

Court: Same ruling. Exception allowed.

Whereupon, respective counsel stated to the court their views as to the nature of the actions involved in this case. At this time the plaintiffs, through their counsel, stipulated that their [157] cause of action was of an equitable nature.

At this time the defendants, through their counsel, stipulated that their cause of action was of an equitable nature but would not stipulate that the plaintiffs' cause of action was of an equitable nature.

At this time, the Court discharged the Jury from further consideration of this case.

The foregoing was all of the evidence presented by the plaintiffs and the defendants in the cause, and counsel for the plaintiffs and for the defendants thereupon presented their oral arguments to the Court.

Thereafter, and on the 4th day of January, 1943 the Court did make and order entered its Findings of Fact and Conclusions of Law; to each of which the defendants excepted and exception was allowed by the Court.

And thereafter, and on the 4th day of January, 1943 the Court did sign and order entered its decree, to which the defendants excepted and the exception was allowed by the Court.

For as much as the matters and things above set forth do not fully appear of record, the said defendants A. T. Martin and Alice M. Martin tender and present as their Bill of Exceptions in said cause, and pray that the same be settled, allowed, signed and sealed and made a part of the record in said cause by this court, pursuant to law in such cases.

Dated at Anchorage, Alaska this 21st day of September, 1943.

THOMAS M. DONOHOE
JOHN E. MANDERS
Attorneys for defendants

[Endorsed]: Filed Dec. 17, 1943. [158]

[Title of District Court and Clause.]

ACKNOWLEDGMENT OF SERVICE

Receipt is hereby acknowledged of copy of Statement of Evidence and Bill of Exceptions on appeal in the above entitled action.

Dated at Anchorage, Alaska, this 21st day of September, 1943.

W. N. CUDDY
Of Attorneys for Plaintiffs.

[Endorsed]: Filed Dec. 17, 1943. [159]

[Title of District Court and Cause.]

ORDER EXTENDING TERM OF COURT FOR PURPOSE OF PRESENTATION, SETTLEMENT AND ALLOWANCE OF BILL OF EXCEPTIONS

This matter coming on for hearing this day upon the application of defendants A. T. Martin and Alice M. Martin requesting that the present term of the above entitled court be continued for the purpose of presentation, settlement and allowance of the Bill of Exceptions in the above entitled cause; it is hereby

Ordered, that the present term of the above entitled court be, and the same hereby is, extended to and including the 15th day of December, 1943 within which to present, settle and allow the Bill of Exceptions and perfect the appeal of defendants in the above entitled action.

Made and Ordered Entered at Anchorage, Alaska, this 16th day of October, 1943.

SIMON HELLENTHAL
District Judge

[Endorsed]: Filed Oct. 16, 1943. [160]

[Title of District Court and Cause.]

ORDER EXTENDING TIME FOR SETTLING BILL OF EXCEPTIONS

This matter coming on for hearing this day upon the application of the defendants A. T. Martin and

Alice M. Martin, requesting sixty (60) days additional time to prepare present and file the record on appeal in the above-entitled cause, and to settle the bill of exceptions; it is hereby

Ordered, that the defendants have sixty (60) days additional time, to-wit, to and including the 15th day of December, 1943, within which to prepare, file, present or have approved the record and bill of exceptions in the above entitled cause.

Made and Ordered Entered at Anchorage, Alaska, this 16th day of October, 1943.

SIMON HELLENTHAL
District Judge

[Endorsed]: Filed Oct. 16, 1943. [161]

[Title of District Court and Cause.]

ACKNOWLEDGMENT OF SERVICE

Receipt is hereby acknowledged of copy of each of the following documents on appeal in the above entitled action:

1. Order Extending Time For Settling Bill Of Exceptions
2. Order Extending Term Of Court For Purpose Of Presentation, Settlement and Allowance Of Bill Of Exceptions.

Dated at Anchorage, Alaska, this 16th day of October, 1943.

W. N. CUDDY
Of Attorneys for Plaintiffs.

[Endorsed]: Filed Dec. 17, 1943. [162]

[Title of District Court and Cause.]

STIPULATION

It Is Hereby Stipulated And Agreed by and between counsel for the plaintiffs and defendants above named, that the foregoing condensed and narrative statement of the evidence is a true and accurate statement of all the evidence introduced at the trial of the cause, and is hereby approved.

It is further stipulated and agreed that the said statement of evidence and bill of exceptions may be brought on for hearing without further notice; that an immediate hearing may be had upon upon the same, and that the same may be approved and settled as a statement of the evidence and bill of exceptions immediately without further notice.

Dated at Anchorage, Alaska, this 16th day of December, 1943.

W. N. CUDDY
Of Attorneys for Plaintiffs
JOHN E. MANDERS
Of Attorneys for Defendants

[Endorsed]: Filed Dec. 17, 1943. [163]

[Title of District Court and Cause.]

ORDER APPROVING AND CERTIFYING STATEMENT OF THE EVIDENCE AND SETTLING BILL OF EXCEPTIONS

A. T. Martin and Alice M. Martin having applied to the Court for an order approving and certifying the statement of evidence filed in this cause and

settling the same as a bill of exceptions to be used on their appeal to the United States Circuit Court of Appeals for the Ninth Circuit, from the decree entered herein on the 4th day of January, 1943; and it appearing that the plaintiffs and defendants, by and through their respective counsel, have stipulated that said statement of the evidence and bill of exceptions is a true and accurate statement of all of the evidence introduced in the trial of the cause, and having stipulated and agreed that the said statement of the evidence and bill of exceptions may be brought on for hearing without further notice, and that an immediate hearing may be had upon the same, and that the same may be approved and settled immediately without further notice; and it further appearing that said bill of exceptions contains a condensed narrative statement of the evidence in the cause, and is complete and correct; and the Court having examined the said statement of the evidence and bill of exceptions, and being fully advised in the premises, it is, therefore,

Ordered, that said statement of the evidence and bill of [164] exceptions be, and the same hereby is, approved and settled as a bill of exceptions upon the appeal of the defendants to the United States Circuit Court of Appeals for the Ninth Circuit, and

It is further ordered that this order shall be deemed and taken as a certificate of the undersigned judge of this court who presided at the hearing of the said cause and before whom all the evidence in said cause was given, that the said bill of exceptions contains a condensed statement in narrative

form of all the evidence given in said cause, including exhibits introduced by the parties, and upon which the said decree of January 4, 1943 is based.

Done by the Court and ordered entered, this 17th day of December, 1943.

SIMON HELLENTHAL
District Judge

[Endorsed]: Filed Dec. 17, 1943. [165]

[Title of District Court and Cause.]

STIPULATION IN RE PRINTING OF RECORD

It Is Hereby Stipulated And Agreed by and between counsel for plaintiffs and defendants that in printing the record of this case upon appeal to the United States Circuit Court of Appeals for the Ninth Circuit, all captions shall be omitted after the title of the cause has once been printed and the words "title of court and cause" and the name of the paper or document shall be substituted therefor.

It Is Further Stipulated And Agreed that the conditional sales agreement, Exhibit "A", the lease, Exhibit "B", the grazing permit, Exhibit "C" and the guaranty, Exhibit "D", copies of which are attached to the complaint and various other pleadings in the action instead of being printed as exhibits to each of said pleadings need be printed only once. All other parts of the record shall be printed.

Dated this 16th day of December, 1943.

W. N. CUDDY
Of Attorneys for Plaintiffs
JOHN E. MANDERS
Of Attorneys for Defendants

[Endorsed]: Filed Dec. 17, 1943. [166]

[Title of District Court and Cause.]

ORDER EXTENDING TIME FOR SETTLING BILL OF EXCEPTIONS

This matter coming on for hearing this day upon the application of the defendants A. T. Martin and Alice M. Martin, requesting an extension of time to and including the 1st day of February, 1944 within which to prepare, present and file the record on appeal in the above-entitled cause and to settle the Bill of Exceptions; it is hereby

Ordered, that the defendants have additional time, to-wit, to and including the 1st day of February, 1944 within which to prepare, file, present or have approved the record and Bill of Exceptions in the above entitled cause.

Made and ordered entered at Anchorage, Alaska, this 11 day of December, 1943.

SIMON HELLENTHAL
District Judge

[Endorsed]: Filed Dec. 11, 1943. [167]

[Title of District Court and Cause.]

ORDER EXTENDING TERM OF COURT FOR PURPOSE OF PRESENTATION, SETTLEMENT AND ALLOWANCE OF BILL OF EXCEPTIONS

This matter coming on for hearing this day upon the application of defendants A. T. Martin and Alice M. Martin requesting that the Special Anchorage October 1942 Term of the above entitled court be continued for the purpose of presentation, settlement and allowance of the Bill of Exceptions in the above entitled cause; it is hereby,

Ordered, that the Special Anchorage October 1942 Term of the above entitled court be, and the same hereby is, extended to and including the 1st day of February, 1944 within which to present, settle and allow the Bill of Exceptions and perfect the appeal of defendants in the above entitled action.

Made and ordered entered at Anchorage, Alaska, this 11th day of December, 1943.

SIMON HELLENTHAL
District Judge

Entered Court Journal No. G-7 Page No. 342 Dec 11 1943

[Endorsed]: Filed Dec. 11, 1943. [168]

[Title of District Court and Cause.]

ACKNOWLEDGMENT OF SERVICE

Receipt is hereby acknowledged of copy of each of the following documents on appeal in the above entitled action:

1. Order Extending Time For Settling Bill of Exceptions
2. Order Extending Term of Court For Purpose of Presentation, Settlement and Allowance of Bill of Exceptions.

Dated at Anchorage, Alaska, this 13th day of December, 1943.

W. N. CUDDY
Of Attorneys for Plaintiffs.

[Endorsed]: Filed Dec. 17, 1943. [169]

[Title of District Court and Cause.]

STIPULATION FOR PRAECIPE

To the Clerk of the District Court
For the Territory of Alaska,
Third Division.

It Is Hereby Stipulated And Agreed by and between counsel for the respective parties hereto that the record on appeal shall consist of, and that you will please make, certify and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, at San Francisco, California, a true copy of each of the following indicated portions

of the record in the above entitled action as the transcript to be used on the appeal of A. T. Martin and Alice M. Martin, defendants, from the decree rendered herein on the 4th day of January, 1943, to-wit:

(1) Complaint
(2) Demurrer
(3) Minute Order Overruling Demurrer
(4) Answer
(5) Motion and Order to Amend Complaint
(6) Minute Order Granting Leave to Move Against Certain Papers
(7) Amended Complaint
(8) Reply [170]
(9) Motion to Strike Amended Complaint
(10) Minute Order Denying Motion to Strike
(11) Demurrer to Amended Complaint
(12) Minute Order Overruling Demurrer
(13) Minute Order Granting Defendants Leave Plead Estoppel
(14) That part of the Journal showing trial by Jury December 21, 1942 which shows the objection of defendants to the testimony of Earl Francis Graves; and also that part of the same Journal showing the objection of the defendants to any evidence produced in this case
(15) Findings of Fact and Conclusions of Law
(16) Decree
(17) Motion for New Trial

(18) Minute Order Overruling Motion for New Trial, dated June 3, 1943
(19) Petition for Appeal
(20) Assignment of Errors
(21) Order Allowing Appeal
(22) Citation on Appeal
(23) Bond on Appeal
(24) Acknowledgment of Service of Appeal Papers
(25) Order Extending Time for Settling Bill of Exceptions
(26) Statement of Evidence and Bill of Exceptions
(27) Acknowledgment of Service
(28) Order Extending Term of Court for purpose of Presentation, Settlement and Allowance of Bill of Exceptions
(29) Order Extending Time for Settling Bill of Exceptions
(30) Acknowledgment of Service
(31) Stipulation in re Statement of Evidence and Bill of Exceptions
(32) Order Approving and Certifying Statement of Evidence and Settling Bill of Exceptions [171]
(33) Stipulation in re Printing of Record
(34) Order Extending Time for Settling Bill of Exceptions
(35) Order Extending Term of Court for Purpose of Presentation, Settlement and Allowance of Bill of Exceptions
(36) Acknowledgment of Service

(37) This Stipulation for Praecipe
(38) Praecipe for Transcript on Appeal from Judgment
(39) Clerk's Certificate

It is further stipulated and agreed that such additional portions of the record as may be required by either plaintiffs or defendants may be certified and transmitted.

Dated this 16th day of December, 1943.

W. N. CUDDY
Of Attorneys for Plaintiffs
JOHN E. MANDERS
Of Attorneys for Defendants

[Endorsed]: Filed Dec. 17, 1943. [172]

[Title of District Court and Cause.]

PRAECIPE FOR TRANSCRIPT ON APPEAL FROM JUDGMENT

To the Clerk of the District Court
For the Territory of Alaska
Third Judicial Division

You are hereby requested, in transmitting a true copy of the record of the District Court for the Territory of Alaska, Third Division, in the above entitled cause pursuant to the appeal of the defendants and appellants from the judgment entered on the 4th day of January, 1943, to incorporate into the transcript of record on such appeal the following portions of the record in said cause in your office, to-wit:

(1) Complaint

(2) Demurrer

(3) Minute Order Overruling Demurrer

(4) Answer

(5) Motion and Order to Amend Complaint

(6) Minute Order Granting Leave to Move against Certain Papers

(7) Amended Complaint

(8) Reply

(9) Motion to Strike Amended Complaint

(10) Minute Order Denying Motion to Strike

(11) Demurrer to Amended Complaint [173]

(12) Minute Order Overruling Demurrer

(13) Minute Order Granting Defendants Leave to Plead Estoppel

(14) That part of the Journal showing trial by Jury December 21, 1942 which shows the objection of defendants to the testimony of Earl Francis Graves; and also that part of the same Journel showing the objection of the defendants to any evidence produced in this case

(15) Findings of Fact and Conclusions of Law

(16) Decree

(17) Motion for New Trial

(18) Minute Order Overruling Motion for New Trial, dated June 3, 1943.

(19) Petition for Appeal

(20) Assignment of Errors

(21) Order Allowing Appeal

(22) Citation on Appeal

(23) Bond on Appeal

(24) Acknowledgment of Service on Appeal Papers

(25) Order Extending Time for Settling Bill of Exceptions

(26) Statement of Evidence and Bill of Exceptions

(27) Acknowledgment of Service

(28) Order Extending Term of Court for purpose of presentation, settlement and allowance of Bill of Exceptions

(29) Order Extending Time for Settling Bill of Exceptions

(30) Acknowledgment of Service

(31) Stipulation in re Statement of Evidence and Bill of Exceptions

(32) Order Approving and Certifying Statement of Evidence and Settling Bill of Exceptions

(33) Stipulation in re Printing of Record

(34) Order Extending Time for Settling Bill of Exceptions [174]

(35) Order Extending Term of Court for Purpose of Presentation, Settlement and Allowance of Bill of Exceptions

(36) Acknowledgment of Service

(37) Stipulation for Praecipe

(38) This Praecipe for Transcript on Appeal from Judgment

(39) Clerk's Certificate

Dated, this 16th day of December, 1943.

THOMAS M. DONOHOE and
JOHN E. MANDERS
Attorneys for defendants and
appellants.

Receipt of a copy of the foregoing Praecipe is hereby acknowledged this 16th day of December, 1943.

W. N. CUDDY
of Attorneys for Plaintiffs

[Endorsed]: Filed Dec. 17, 1943. [175]

CERTIFICATE OF CLERK TO TRANSCRIPT OF RECORD

United States of America,
Territory of Alaska,
Third Division—ss.

I, M. E. S. Brunelle, Clerk of the District Court for the Territory of Alaska, Third Division, do hereby certify that the foregoing and hereto annexed 175 pages, numbered from 1 to 175, inclusive, are a full, true and correct transcript of the records and files of the proceedings in the above entitled cause, made in accordance with the praecipe filed in my office on the 17th day of December, 1943, as the same appears on the records and files in my office; that the foregoing transcript has been prepared, examined and certified to by me, and that the costs thereof, amounting to $26.50, has been

paid to me by John E. Manders, of counsel for the appellants herein.

In testimony whereof, I have hereunto set my hand and affixed the seal of said Court this 11th day of January, 1944.

[Seal] M. E. S. BRUNELLE
Clerk of the District Court, Territory of Alaska, Third Division.

[Endorsed]: No. 10665. United States Circuit Court of Appeals for the Ninth Circuit. A. T. Martin and Alice M. Martin, Appellants, vs. Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and Ross L. Sheely, Copartners, Appellees. Transcript of Record. Upon Appeal from the District Court for the Territory of Alaska, Third Division.

Filed January 19, 1944.
PAUL P. O'BRIEN
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

No. 10,665

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

A. T. MARTIN and ALICE M. MARTIN,
Appellants,

vs.

CHARLOTTE L. SHEELY, JOHN H. SHEELY, JOE A. SHEELY and ROSS L. SHEELY, co-partners,
Appellees.

Upon Appeal from the District Court for the Territory of Alaska, Third Division.

BRIEF FOR APPELLANTS.

THOMAS M. DONOHOE,
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For the Ninth Circuit

A. T. MARTIN and ALICE M. MARTIN,
Appellants,

vs.

CHARLOTTE L. SHEELY, JOHN H. SHEELY, JOE A. SHEELY and ROSS L. SHEELY, co-partners,
Appellees.

Upon Appeal from the District Court for the Territory of Alaska, Third Division.

BRIEF FOR APPELLANTS.

STATEMENT OF THE CASE.

Prior to June 26, 1941 appellants owned and operated a dairy and milk distribution business at and around Anchorage, Alaska and on that date entered into an agreement for the sale of the personal property used in said business and the leasing of the real estate upon which it was situated, together with a grazing permit upon certain other lands, with appellees Charlotte L. Sheely, John H. Scheely and Joe A. Sheely. On the same date appellee Ross L. Sheely guaranteed in writing the performance of these contracts.

This litigation arises out of plaintiffs' and appellees' contention that certain livestock involved in the contract of sale was infected with Bang's disease at the time of the sale and that this was known to appellants and not to appellees. Appellants, on the other hand, contend that the property was purchased by said appellees specifically without any warranties whatsoever as to the condition of the livestock and after inspection by the appellees.

Appellees' complaint, filed May 13, 1942, alleges briefly:

That as a result of certain oral negotiations plaintiffs and appellees Charlotte L. Sheely, John H. Sheely, Joe A. Sheely and the defendants-appellants made and executed a conditional sales agreement, a lease and a grazing permit (R. 2-3) copies of which are set out in full as exhibits, and that each of these instruments was a part of the whole transaction. Under the conditional sales agreement appellants agreed to sell and said appellees agreed to purchase

> "The whole of that dairy and milk distribution business now being conducted by the sellers under the trade name and style of Step And Half Ranch at and around Anchorage, Alaska, save and except the accounts receivable of the sellers but including the livestock, furniture and fixtures, farming implements and tools and motive equipment that are set forth and particularly described in the hereto attached inventory marked exhibit 'A' which is by reference incorporated in and made a part of this description; and also including the good will of the sellers in and to said dairy and milk distribution business"

for the sum of $28,294.00 payable $9800.00 in cash and the balance at the rate of $308.22 on the 10th day of each month commencing on August 10, 1941, together with interest at six percentum from the 1st day of July, 1941 until paid. (R. 10-11.) Paragraph Sixth of said conditional sales agreement reads as follows:

> "Sixth. It is understood and expressly agreed that the buyers have inspected the property covered by this agreement and are familiar with the condition thereof and that the same is sold to the buyers without any warranties or representations of any kind or character whatsoever on the part of the sellers, save and except that the sellers warrant and agree that they are the lawful owners thereof and have full right, power and authority to sell and dispose of the same and that there are no existing liens or encumbrances against said property or any part or portion thereof." (R. 13.)

Exhibit "A" attached to this conditional sales agreement embraces 99 classifications of property of which the first two are "56-Cows, 1-Bull". (R. 17-20.) In the lease appellants leased to said appellees certain real estate situated in Anchorage Precinct, Territory of Alaska, for a term of ten years commencing with July 1, 1941 at the monthly rental of $200.00 per month in advance. (R. 21-26.) By the grazing permit appellants granted permission to said appellees to graze over certain lands leased by appellant A. T. Martin from the Territory of Alaska upon the payment of the sum of $110.00 per year. (R. 27-28.)

Appellees further allege that the principal item of property in the conditional sales agreement was 56

head of cows and that they were figured at $300.00 per head, amounting to $16,800.00 as the purchase price; that the said appellees paid over $9800.00 under the conditional sales contract, $200.00 on the lease and $110.00 on the grazing permit, and entered into possession on July 1, 1941. (R. 3-4.) That on June 28, 1941, the day of the execution of the sales contract, lease and grazing permit appellee Ross L. Sheely in writing guaranteed the performance of the conditional sales agreement and lease (R. 4, 28-29); that appellees have performed to date the terms and conditions of these several agreements and in addition to the payments previously named have paid $1541.10 on principal and $450.00 interest on the conditional sales agreement, $1000.00 under the lease, $550.00 for an equity in a truck being purchased at the time of sale by appellants from a third party, $2000.00 for hay and grain on order at that time, and have purchased additional equipment and have made improvements on the premises at a cost of $2513.00. (R. 5.) That at the time of the execution of the conditional sales agreement a large number of the cows were infected with Bang's disease which was known to appellants and unknown to appellees and that appellants sold the same to appellees with the intent to injure appellees; that since June 28, 1941 appellees have of necessity and because of said disease killed and disposed of 8 of said cows and received therefor the sum of $832.45, one-third the value of uninfected dairy cows; that the cows were purchased for a dairy herd and because of said disease were of little value for such purposes; that the plain-

tiffs and appellees have suffered damage by reason of said wrongful acts and omissions and will suffer irreparable damages if they are required to perform their agreements. (R. 5-6.) A second cause of action is set up in the complaint but as plaintiffs and appellees dismissed as to this at the time of trial, it is not considered necessary to set up the allegations. In their prayer plaintiffs and appellees pray that the conditional sales agreement, grazing permit and guaranty be rescinded, cancelled and declared void; that they have judgment for $16,163.10. (R. 8.)

To this complaint the defendants and appellants demurred upon the grounds that the same did not state facts sufficient to constitute a cause of action and upon the overruling of this demurrer filed their answer generally admitting the execution of the various instruments, denying that there was any segregation in value for the cows, denying that plaintiffs and appellees relied upon any representations of defendants and appellants, denying that plaintiffs and appellees have performed to date the requirements in said conditional sales agreement; denying that they have made improvements at a cost of $2513.00 or any sum, alleging that plaintiffs and appellees have not made any payments due under any of said instruments subsequent to December, 1941, and by reason thereof are in default, and denying that any cows were killed because of necessity or because of said disease; and generally defendants and appellants denied the other allegations of plaintiffs' and appellees' complaint alleging any misconduct on their part. (R. 30-33.)

As a first counterclaim and cross-complaint defendants and appellants alleged the execution of the conditional sales agreement referred to in plaintiffs' and appellees' complaint, further alleged that plaintiffs and appellees have defaulted for failure to make the payments due in January, 1942 and thereafter; that plaintiffs and appellees permitted other persons to have possession and control of the property and that plaintiffs and appellees contrary to the terms of the agreement have not maintained the dairy herd in an equivalent number; that there is due from plaintiffs and appellees to defendants and appellants the sum of $16,952.90 together with interest at 6% per annum from December 10, 1941 upon said conditional sales agreement. (R. 34-37.) For a second counterclaim and cross-complaint defendants and appellants alleged the execution of the lease mentioned in plaintiffs' and appellees' complaint; alleged that Ross L. Sheely guaranteed in writing the payment of the rentals named therein; alleged that the plaintiffs and appellees have refused to pay the rentals for the months January to October inclusive, 1942, and that by reason thereof there is due defendants and appellants the sum of $2000.00 together with interest at 6% per annum and that under the terms of the lease defendants and appellants elected to obtain immediate possession of said premises. (R. 37-38.) For a third counterclaim and cross-complaint defendants and appellants alleged the execution of the grazing permit mentioned in said plaintiffs' and appellees' complaint; that plaintiffs and appellees refused to make the payment of $110.00 due August 19, 1942 and are in default; and that defend-

ants and appellants were entitled to immediate possession. By way of prayer defendants and appellants prayed that plaintiffs and appellees take nothing by reason of their complaint; that defendants and appellants have judgment for the sum specified in their first and second cross-complaints and have possession of the premises mentioned in their third cross-complaint. (R. 39-40.)

At the time of the trial on December 18, 1942 plaintiffs and appellees moved the court for permission to amend their complaint by adding to the title the words "copartners" and that the other allegations of the complaint be likewise amended to show the copartnership. This was granted by the court and defendants and appellants were given time to move against such amended complaint and reply when filed. It is to be noted that no reply whatsoever had been filed at the time the court started trial of this case. The actual trial was commenced on December 19, the amended complaint and a reply were filed on December 21, after the trial had been going on for several days. The amended complaint filed by the plaintiffs and appellees contained similar allegations to those contained in the original complaint, except they alleged that on June 28, 1941 plaintiffs and appellees were copartners, and in addition contained paragraph XI alleging that plaintiffs and appellees had suffered damages in the sum of $15,000.00 by reason of the wrongful acts and omissions of defendants; and the prayer in this instance was for judgment against defendants and appellants in the sum of $15,000.00 in

addition to having the various instruments declared illegal and void. (R. 45-53.)

The reply of plaintiffs and appellees alleged the co-partnership mentioned above and as an affirmative defense set up practically the identical allegations contained in the complaint. (R. 53-59.)

On the same day the defendants and appellants moved to strike the amended complaint upon the ground that it did not conform to the order of the court permitting amendments, which motion was denied and excepted to. On the same day the defendants and appellants demurred to the amended complaint upon the ground that the same did not state facts sufficient to constitute a cause of action; which demurrer was overruled and the order was excepted to. On the same date the court by order directed that defendants' and appellants' original answer would apply to plaintiffs' and appellees' amended complaint and that the defendants and appellants likewise should have the right to plead estoppel. (R. 60-63.)

The trial of the action was commenced on December 19 as a law case with a jury but at the conclusion of the plaintiffs' and appellees' case and after the defendants and appellants had moved for the granting of a nonsuit, plaintiffs and appellees abandoned this position; the court dismissed the jury and the trial proceeded as an equity case.

ASSIGNMENT OF ERRORS.

The following assignment of errors will be relied upon:

1. The court erred in overruling the demurrer of defendants to the complaint of the plaintiffs on file herein upon the grounds that the same does not state facts sufficient to constitute a cause of action, which ruling was duly excepted to by the defendants herein and exception allowed. (R. 79.)

2. The court erred in granting the motion for leave to amend complaint by the plaintiffs to incorporate therein that plaintiffs were a partnership including plaintiff Ross L. Sheely, the granting of which order was duly excepted to and exception allowed. (R. 80.)

3. The court erred in denying defendants' motion to strike plaintiffs' amended complaint upon the ground that the same did not conform to the order of the court permitting amendment, which was duly excepted to and exception allowed. (R. 80.)

4. The court erred in overruling the demurrer to plaintiffs' amended complaint upon the grounds that the same did not state facts sufficient to constitute a cause of action, which order was duly excepted to and exception allowed. (R. 80.)

5. The court erred in denying defendants' objection to any testimony in support of plaintiffs' amended complaint, as shown by the objection to the testimony of plaintiffs' witness Earl Francis Graves, as follows:

"Q. (by Mr. Cuddy). I will ask you whether or not during the month of April, 1941, you examined the dairy herd of A. T. Martin?

Mr. Donohoe. Objected to—the first cause of action does not state facts sufficient to constitute a cause of action, and the second cause of action does not state a cause of action and they have been improperly united.

Court. Motion overruled. Exception granted.

Donohoe. That will go to all this evidence. We object to the testimony of this witness, as to the examination of the herd—it cannot vary the terms of the contract Exhibit 'A'—the conditional sales contract involved herein.

Court. Motion overruled. Exception allowed."

The witness was then permitted to testify as to the condition of the herd as to Bang's disease. (R. 80-81.)

6. The court erred in denying motion for nonsuit made by the defendants at the close of plaintiffs' case upon the grounds that the complaint does not state facts sufficient to constitute a cause of action, and upon the further grounds that there is not sufficient evidence to sustain the allegations of plaintiffs' complaint, to which ruling defendants excepted and exception was allowed. (R. 81.)

7. The court erred in dismissing the jury and considering this cause as one of an equitable nature, over the objection of the defendants, to which ruling the defendants excepted and the exception was allowed. (R. 81.)

8. The court erred in refusing to allow defendants' motion for a nonsuit at the close of the trial of this action, upon the grounds that the complaint does not state facts sufficient to constitute a cause of action and that there is not sufficient evidence to sustain the

allegations of plaintiffs' complaint, to which ruling defendants excepted and exception was allowed. (R. 81.)

9. The court erred in overruling defendants' objection to the introduction of Plaintiffs' Exhibit "C" introduced on the redirect examination of Earl Francis Graves, as follows:

"Donohoe. Object to the offer, it is too remote and not pertaining to the issues of this case.

Court. Objection overruled. Exception allowed."

The offer is received and marked Plaintiffs' Exhibit "C", being a report dated March 7, 1941.

Exhibit "C" being a record of the condition of Mr. Sheely's herd at Palmer, Alaska, was then received. (R. 81-82.)

10. The court erred in refusing to strike plaintiffs' Exhibit "C" introduced on the redirect examination of Earl Francis Graves, as follows:

"Q. (by Mr. Donohoe). Are you sure that paper is the same as you prepared it on March 7, 1941, did you write that on there yourself?

A. No, that has been put on later.

Donohoe. We move to strike.

Court. I think the writing on the side should be stricken from that exhibit.

Donohoe. We move to strike the exhibit.

Court. The writing may be taken off.

Donohoe. Exception.

Court. Exception allowed. * * *

Donohoe. In order to keep the record straight we have to show what is on that exhibit.

Court. The record may show butchered was written on in two places after the report was made. The Court ruled that they may be stricken.

Donohoe. Exception. The exhibit is not as originally prepared and will have undue influence upon the jury in the trial of this case.

Court. No objection was made at the time the exhibit was offered on account of those words being there. Exception allowed."

The exhibit was the same Exhibit "C", being a record of the condition of Mr. Sheely's herd of cows at Palmer, Alaska. (R. 82-83.)

11. The court erred in overruling defendants' objection to questions asked plaintiffs' witness Ross L. Sheely on direct examination, as follows:

"Q. (by Mr. Cuddy). I notice in Exhibits "A", "B" and "C" that your name is not on the list, not a signature to it but as a guaranty, will you explain to the jury how that situation arose?

Donohoe. Objected to as incompetent, the pleadings and exhibits speak for themselves.

Court. Objection overruled. Exception granted."

Mr. Sheely was then permitted over objection to testify that he was operating as a copartner with the other members of the family and his reasons for having a copartnership, contrary to the original agreements entered into between plaintiffs and defendants herein. (R. 83.)

12. The court erred in sustaining plaintiffs' objection to the question asked plaintiffs' witness Ross L. Sheely on cross-examination, as follows:

"Q. (by Mr. Donohoe). How much have you received from the butchered calves?

Grigsby. Objected to as immaterial.

Court. I will not go into the increase. Exception allowed.

Q. How much have you received from the sale of milk from these cows?

Grigsby. Objected to.

Court. Objection sustained. Exception granted."

The court refused to permit defendants to prove the value of the milk products sold by plaintiffs, derived from said dairy herd and also refused to permit defendants to prove the value of the calves born to said dairy cows and received by plaintiffs, and the court refused to permit defendants to prove the value of other products sold from the ranch premises and received by plaintiffs. (R. 83-84.)

13. The court erred in refusing to grant the motion of the defendants to strike the testimony of plaintiffs' witness Ross L. Sheely as to improvements made to the premises and as to what was a reasonable value for rental of the land, contrary to the amount agreed upon in the written lease, and as to the individual value of cows, and money spent by the witness Ross L. Sheely, as follows:

"Donohoe. I couldn't very well object to the questions of the Court, but if your Honor please I move to strike the answers of the witness as incompetent, irrelevant and immaterial.

Court. Motion denied.

Donohoe. I also object to the testimony of this witness as to monies spent by this witness as incompetent. This witness was not a party to this contract.

Court. Was this money paid under the contract?

A. Yes, sir.

Q. And you know it was paid under the contract?

A. Yes, sir.

Court. Motion overruled. Exception allowed.

Donohoe. He testified he paid it.

Grigsby. On whose behalf was this money paid—on your part or on the part of the copartnership?

Donohoe. Object, there is no mention of a copartnership in the agreement.

Court. You may have an exception." (R. 84-85.)

14. The court erred in overruling defendants' objection to the question asked plaintiffs' witness Charlotte Sheely on direct examination, as follows:

"Q. (by Mr. Cuddy). Covering the purchase of cattle on the Martin ranch and a lease of the property on behalf of whom were those three signatures?

Donohoe. Object as incompetent. The papers speak for themselves.

Court. She say testify. Exception allowed.

A. I signed it for the copartners, the four, Mr. Sheely, myself, Jack and Joe." (R. 84-85.)

15. The court erred in overruling defendants' objection to the question asked plaintiffs' witness John H. Sheely on direct examination, as follows:

"Q. (by Mr. Cuddy). And in whose benefit did you sign such instrument?

Donohoe. Object to the question.

Court. Objection overruled.

Q. For whose benefit did you sign that agreement?

Donohoe. Object as incompetent, the papers speak for themselves.

A. Well, I signed it on behalf of—we were planning a partnership, we were going to work it on shares." (R. 85-86.)

16. The court erred in finding:

(a) As in its first findings of fact, that on the 26th day of June, 1941, plaintiffs were copartners;

(b) As in its second findings of fact, that on said 26th day of June, 1941, plaintiffs Charlotte L. Sheely, John H. Sheely and Joe A. Sheely "on behalf of said partnership", entered into certain contracts, copies of which are attached to the amended complaint marked Exhibits "A", "B" and "C";

(c) As in its third findings of fact, "That at various times prior to January, 1942, the plaintiffs paid for permanent improvements to said dairy ranch and for durable supplies and equipment the sum of $1766.85 * * *";

(d) As in its fourth findings of fact, "That at the time said plaintiffs entered into said agreement and at the time said plaintiffs entered into possession of said premises, and for a long time prior thereto, a large number of the cows sold to the plaintiffs and described in the said conditional sales contract were diseased and infected with Bang's disease or contagious abortion, which fact was well known to the defendants and unknown to the plaintiffs; that not-

withstanding such knowledge upon the part of the defendants and without disclosing the same to the plaintiffs, the defendants sold and delivered the said premises and livestock thereon to the plaintiffs and accepted from the plaintiffs a portion of the purchase price thereof as hereinabove alleged";

(e) As in its fifth findings of fact, that 36 of said cattle "became useless for dairy purposes and plaintiffs were compelled on that account to slaughter and sell the same for beef, from which sale the plaintiffs derived the sum of $4472.20; that 6 of said cows died on account of said disease and there are 14 cows and one bull left of the original herd, on the premises".

And to each of which said findings defendants excepted and said exceptions were allowed. (R. 86-87.)

17. The court erred in forming its conclusions of law, as follows:

(a) Conclusion of Law No. I: "That the aforesaid conditional sales agreement, lease and grazing permit constituted one transaction and were illegal, against public policy and prohibited by Section 2 of Chapter 55 of the Session Laws of Alaska, 1919. (Sec. 626, Compiled Laws of Alaska, 1933.)"

(b) Conclusion of Law No. II: "That the plaintiffs are entitled to recover from the defendants the sum of $14,867.95, being moneys paid and expended as set forth in paragraph III of the Findings of Fact herein, together with interest on the various payments and expenditures from the time made, amounting in all to the sum of $16,091.89; that from this sum the

defendants are entitled to deduct in the sum of $4472.20, leaving the balance due from defendants to plaintiffs of the sum of $11,619.69, for which plaintiffs are entitled to judgment against the defendants."

(c) Conclusion of Law No. III: "That the plaintiffs are entitled to dispose of the 12 cows now on the Step-And-Half Ranch belonging to them, either by slaughtering or otherwise as may be permitted by law."

(d) Conclusion of Law No. IV: "That said conditional sales agreement, lease agreement and assignment of grazing permit should be rescinded."

(e) Conclusion of Law No. V: "That the defendants are entitled to immediate possession of the said premises constituting the Step-And-Half Ranch and the livestock and personal property thereon, except the said 12 cows belonging to plaintiffs, to the possession of the land described in the said lease agreement and to the use of the area described in said grazing permit."

To each of which conclusions of law defendants excepted and said exceptions were allowed. (R. 87-88.)

18. The court erred in rendering its decree for the plaintiffs herein. The court's error in this regard was based upon the following errors of the court occurring during the trial of the case: All of the errors herein assigned, to-wit: Assignments of Error 1 to 17 inclusive.

ARGUMENT.

For the purpose of convenience the argument can be broken down into a few general subheadings:

1. Neither the complaint nor the amended complaint stated facts sufficient to constitute a cause of action.

(a) The statute upon which plaintiffs and appellees based their complaint and amended complaint is unconstitutional.

(b) Even if constitutional it should not be construed to make this contract illegal or to prohibit the ownership or sale of cows unless they have been ordered destroyed by the inspector.

(c) That in other particulars the complaint and amended complaint are fatally defective.

2. The Court erred in rulings as to the admission or rejection of evidence.

3. The findings and decree are not supported by the evidence or justified under the pleadings.

---

1. THE COMPLAINT AND AMENDED COMPLAINT FAIL TO STATE FACTS SUFFICIENT TO CONSTITUTE A CAUSE OF ACTION.

(a) Although not so specified in either the complaint or amended complaint plaintiffs and appellees apparently rely upon the provisions of Chapter 55, Session Laws of Alaska, 1919, as amended by Chapter 7, Session Laws of 1921 and Chapter 64, Session Laws of 1923 (Livestock Inspection Secs. 625, 632 incl., Compiled Laws of Alaska 1933), the pertinent part of which reads as follows:

"Chapter 55, Session Laws of Alaska, 1919. An Act to prohibit the importation into the Territory of Alaska, of diseased livestock, to make provision for the eradication of diseased livestock now in the Territory, and to make appropriation for carrying out the provisions of this Act, and declaring an emergency.

Be it enacted by the Legislature of the Territory of Alaska:

Section 1: Importation of diseased livestock prohibited.

To import or to bring, into the Territory of Alaska, animals of whatsoever kind or character, diseased or infected with the diseases mentioned in Section 3 of this Act, is hereby declared to be injurious to the public health, against public policy illegal, and punishable as herein provided.

Section 2: To keep or transport diseased livestock forbidden.

To own, have in one's possession, sell, transfer, transport, drive or convey, from one section of the Territory to another, animals or livestock of whatsoever kind or character, diseased or infected with the diseases mentioned in Section 3 of this Act, is hereby declared to be injurious to the public health, against public policy, illegal, and punishable as herein provided.

Section 3: Unlawful to import animals infected with diseases named.—Permits.

It shall be unlawful to bring, into the Territory of Alaska, any horses, cattle, or swine, for work, feeding, breeding or dairy purposes, without first

having such animals examined and found free from the following contagious diseases: glanders, farcy, tuberculosis, actinomycosis, rinderpest, foot and mouth disease, contagious abortion, contagious keratitis, scabies, maladie du coit, swine plague and hog cholera, and without having obtained a permit from the Commissioner of Agriculture, the Assistant Commissioner of Agriculture assigned to the division of dairy and livestock of the state, territory or foreign country from which said livestock is shipped, or a permit from an inspector of the Department of Agriculture of the United States assigned to the division of dairy and livestock in the state, territory or foreign country from which such livestock is shipped; and no steamship or transportation company, or other common carrier, shall bring any such animals into the Territory of Alaska without first having had the same examined and found free from said diseases and having obtained the permit herein provided for.

Section 4: Penalties for violation of Statute.

For each evasion or violation of any provision of the three sections last preceding, the shipper or party responsible for the evasion or violation shall be fined not more than $500.00; the consignee knowingly receiving such diseased animals so shipped and transported in violation of said sections, shall be fined not more than $500.00; and the carrier knowingly carrying or transporting the same in violation of said sections, shall be fined not more than $500.00. Actions to enforce the provisions of this Act shall be brought and prosecuted under 'Title XV, Code of Criminal Procedure', Criminal Laws of Alaska, 1913, by the

United States District Attorneys for the Territory of Alaska.

Section 5: Domestic animals to be subject to inspection.

Horses, cattle or swine, for work, feeding, breeding or dairy purposes in the Territory of Alaska shall be subject to inspection and test for all diseases, and to quarantine and destruction where found to be infected with or suffering from any contagious disease by an Inspector of the Bureau of Animal Industry, United States Department of Agriculture, duly assigned by the Chief of the Bureau of Animal Industry to make inspection and test of animals suspected of being diseased in the Territory of Alaska.

Section 6: Inspector to determine whether to quarantine or destroy.

After inspection and test, the Inspector described in Section 5 of this Act shall determine whether the animal inspected is subject to quarantine or to destruction; if to quarantine, he shall prescribe the conditions and the length of time the animal shall be subject to quarantine. Where the Inspector determines that the animal should be destroyed, he is hereby authorized to condemn and cause said animal to be destroyed in such manner as he may determine, but the owner of such animal shall receive the proceeds of the sale of such slaughtered animal, if any.

Section 7: Appropriation.

There is hereby appropriated, out of the money now in the Treasury of the Territory, and not otherwise appropriated, the sum of $2,000.00 to

defray any expenses incurred in the enforcement of this Act, and the Governor of the Territory is hereby empowered, authorized and directed to carry out and to enforce the provisions of this Act; provided, however, that after the expenditure of the said $2,000.00, no further expense in connection with the enforcement of this Act shall be incurred or accrue against the Territory.

Section 8: Emergency.

An emergency is hereby declared to exist, and this Act shall be in force and effect from and after its passage and approval.

Approved May 5, 1919."

Amended by *Chapter 7, Session Laws of 1921,* as follows:

"To amend Sections 5, 6, 7 and 8 of Chapter 55, Alaska Session Laws, 1919, which act relates to diseased livestock; to provide for inspection of livestock and to make provision for carrying out this Act, and declaring an emergency.

Be it enacted by the Legislature of the Territory of Alaska: That Sections 5, 6, 7 and 8 of Chapter 55 of Alaska Session Laws, 1919, be hereby amended to read as follows:

Section 5. Horses, cattle or swine, for work, feeding, breeding or dairy purposes in the Territory of Alaska shall be subject to inspection and test for all diseases, and to quarantine, slaughter or destruction where found to be infected with or suffering from any contagious disease by an Inspector of the Bureau of Animal Industry, United States Department of Agriculture, or by a qualified inspector duly authorized by the Governor of

Alaska to make inspection and tests of animals, in the Territory of Alaska; such inspection and test as far as it relates to animals kept for dairy purposes, by dairies that offer their products to the public generally in the Territory of Alaska and to animals kept for private dairy purposes, provided they are readily accessible, shall be made at least once every year, if possible, and all animals which are not readily accessible for inspection shall be inspected before they are brought into a community where other animals used for dairy purposes are kept, and the Governor of Alaska is hereby authorized to make arrangements with the Bureau of Animal Industry, United States Department of Agriculture, for said inspections and tests; and the Governor is hereby authorized in the event that suitable arrangements can not be made with said Bureau of Animal Industry for the employment or detail of a qualified inspector, to employ one or more competent inspectors to carry out the provisions of this Act. The inspection herein provided for shall be carried on in cooperation with said Bureau of Animal Industry and in accordance with the rules and regulations of said Bureau of Animal Industry.

Section 6. After inspection and test, the Inspector described in Section 5 of this Act shall determine whether the animal inspected is subject to quarantine, slaughter or destruction; if to quarantine he shall prescribe the conditions and the length of time the animal shall be subject to quarantine. Where the Inspector determines that the animal should be slaughtered or destroyed, he is hereby authorized to condemn and cause said animal to be slaughtered or destroyed in such manner as he may determine; in the case of dairy

cattle for which reimbursement only is allowable, such animal shall first be appraised as to its value, determined without regard to the disease of the animal, at a fair valuation by the Inspector and the owner; and where they are unable to agree as to the value of the animal to be slaughtered, the owner and inspector may select a disinterested third party to aid in the appraisement, and where they are unable to agree on the selection of such third party, the United States Marshal, or any of his deputies of the division where the inspection occurs, may designate a third disinterested party to act with the Inspector and owner to determine the value of the animal, as above stated. The amount realized from the sale of the carcass of the slaughtered animal, if any, shall be paid to the owner of such animal and the Inspector shall certify to the Secretary of the Territory the name and address of the owner, the date the animal was condemned, the appraised value of the animal, together with the net sum realized from the salvage thereof, or which could have been realized.

It is further provided, * * *.

Section 7. * * *

Section 8. * * *

Section 9. * * *

Approved April 25, 1921."

Amended by *Chapter 64, Session Laws of 1923,* as follows:

"To amend Chapter 55 of the Alaska Session Laws of 1919, entitled: 'An Act to prohibit the importation into the Territory of Alaska, of dis-

eased livestock, to make provision for the eradication of diseased livestock now in the Territory, and to make appropriation for carrying out the provisions of this Act, and declaring an emergency.'

Be it enacted by the Legislature of the Territory of Alaska:

Section 1. That section three of Chapter 55, Alaska Session Laws of 1919, be amended to read as follows:

'Section 3. It shall be unlawful to bring, into the Territory of Alaska, any horses, cattle, or swine for work, feeding, breeding, dairying, or for any other purposes, without first having such animals examined and found free from the following contagious diseases: glanders, farcy, tuberculosis, actinomycosis, rinderpest, foot and mouth disease, contagious abortion, contagious keratitis, scabies, maladie du coit, swine plague and hog cholera, and without having swine given the serum treatment for hog cholera within two weeks before shipping, unless having obtained a permit from the Commissioner of Agriculture, the Assistant Commisioner of Agriculture assigned to the division of dairy and livestock of the state, territory or foreign country from which said livestock is shipped, or a permit from an inspector of the Department of Agriculture of the United States assigned to the division of dairy and livestock in the state, territory or foreign country from which such livestock is shipped; and no steamship or transportation company, or other common carrier, shall bring any such animals into the Territory of Alaska without having first had the same exam-

ined, or treated, and found free from said diseases and having obtained the permit herein provided for.'

Approved April 30, 1923."

It is the contention of appellants that Section 2 of the Act insofar as it attempts to make illegal the having in one's possession, the selling or transferring of diseased livestock, and in this instance specifically Bang's disease or contagious abortion, is unconstitutional for the reason that the title of the Act embraces more than one subject, and in addition thereto the question of such possession, selling or transferring is not expressed in the title.

The Organic Act of Alaska provides (Sec. 474 CLA 1933), "* * * No law shall embrace more than one subject, which shall be expressed in its title." An examination of the title to this particular Act discloses that it is aimed (a) to prohibit the importation of diseased livestock, and (b) to make provision for the eradication of diseased livestock. A somewhat similar matter was before this court in the case of *Territory of Alaska v. Alaska Juneau Gold Mining Company,* 105 F. (2d) 841, and in the particular statute involved there, there were two subjects embraced in the title the same as in this instance and likewise the court here upheld a similar contention that the Act itself embraced a subject which was not embraced at all in the title. Quoting from the syllabus we find this statement:

"Where title recited that Alaskan act related to compensation for injured employees and bene-

ficiaries in event of death, and title of amendment recited merely that provisions of Compiled Laws relating to 'payment of compensation to injured workmen, etc.' were amended, amendment was invalid to the extent that it purported to require payments to the Territory for the benefit of aged residents, since subject of such provision was unrelated to the subject of compensation to be paid to injured employees or dependents and was not expressed in either title. Comp. Laws Alaska 1933, c. 2161, as amended by Laws Alaska 1935, c. 84; 48 U.S.C.A. § 76."

The court's attention is also directed to the following other cases which merely express the general rule:

The United States v. Howell, 5 Alaska 578, quoting from the syllabus:

"The title of the eight-hour law passed by the Legislature of Alaska in 1913 (Sess. Laws Alaska 1913, c. 29, p. 35) limits its application to lode mining claims. The Act of 1915 (Sess. Laws Alaska 1915, c. 6, p. 6) amending the same, extended its provisions to underground placer mining claims, but without any change or extension of the title of the amending act. Held, the amendatory act of 1915, embraces more than one subject, and, the extension to 'underground placer mines' not being expressed in its title, the act, to that extent, is void for conflict with the eighth section of the Organic Act of August 24, 1912 (37 Stat. L. 514, c. 387 (U.S. Comp. St. 1916, § 3535))."

Benedicto v. Porto Rican American Tobacco Company, 256 Fed. 422, the syllabus reads:

> "Under the Organic Law of Porto Rico, Jones Act, § 34 (U.S. Comp. St. 1918, § 3803n), inhibiting a bill containing more than one subject, which shall be clearly expressed in the title, and providing that an act embracing a subject not expressed in the title shall be void as to such part, Act Porto Rico Dec. 3, 1917, entitled 'An act to amend' Act March 11, 1915, 'entitled an act to protect Porto Rican cigars from misrepresentation,' by providing for inspection, and issuance of stamps of guaranty, is void as to Section 3, which, contrary to the title, intentionally converts what was simply an inspection law into an inspection law and a revenue law, by providing fees for guaranty stamps, which will yield large surplus revenues."

General Petroleum Company v. Hobson, 23 Fed. (2d) 349, it is stated in the syllabus:

> "St. Cal. 1921, p. 404, relates, as appears from its title, to reservation of minerals in state lands, examination and the granting of permits and leases to prospect for and take such minerals, and the provision of section 13 (p. 410) excluding the right of eminent domain to permittees to condemn right of way over private property is void, as not embraced in the title of the act, as required by Const. Cal. Art. 4, § 24."

And further in this case, the court said at page 350:

> "The defendant asserts that the proviso in section 13, supra, is inoperative because not embraced in the title of the act, as required by section 24,

> article 4 of the state constitution. The subject of legislation, as expressed in the title, is state lands, classification and report, granting permits and leasing, making rules, regulations, etc. Only one class, public property, is mentioned in the title; two classes of property, public property and private property, are treated in the body of the act. The legislature could deal with state property. The title for such purpose is all-embracing, but is silent as to private property, and the purpose to grant a right of eminent domain over private property is not embraced in the title, and, this being in derogation of private right, the right to condemn may not be extended by inference or implication, and such provision must be held inoperative."

It is apparent therefore that the instant statute is invalid for the reason that the title embraces more than one subject, namely, the importation of diseased livestock and the eradication of diseased livestock, and also for the more important reason that the title does not in any manner cover the question of possession, sale or transfer of diseased livestock.

(b) However, for the purpose of this argument, even assuming that the Act itself is valid, then we are faced with the necessity of interpreting it so as not to give an absurd result, which would be the fact if it were taken literally as worded. The general rule as given in 59 *C. J.* at page 964 is as follows:

> "In pursuance of the general object of giving effect to the intention of the Legislature the courts are not controlled by the literal meaning of the

> language of the statute but the spirit or intention of the law prevails over the letter thereof, it being generally recognized that whatever is within the spirit of the statute is within the statute although it is not within the letter thereof, while that which is within the letter although not within the spirit is not within the statute. Effect will be given the real intention even though contrary to the letter of the law. The rule of construction according to the spirit of the law is especially applicable where adherence to the letter would result in absurdity or injustice or would lead to contradictions or would defeat the plain purpose of the act or where the provision was inserted through inadvertence. In following this rule words may be modified or rejected and others substituted, or words and phrases may be transposed so the meaning of general language may be restrained by the spirit or reason of the statute and may be construed to admit implied exceptions. * * *''

This rule was adopted by the United States Supreme Court in the *United States of America v. Jacob Katz,* 46 Sup. Ct. 513, 271 U. S. 354, 70 Law. Ed. 986, in which the court says:

> ''General terms descriptive of a class of persons made subject to a criminal statute may and should be limited where the literal application of the statute would lead to extreme or absurd results and where the legislative purpose gathered from the whole act would be satisfied by a more limited interpretation.''

In examining this particular statute if it were taken literally, we would find the following absurd and con-

tradictory result. By Section 6 of the original act and by Sections 5 and 6 of the amendment of 1921 it is noted that provision is made for the inspection of livestock by an inspector in the Territory of Alaska and that this inspector is given the specific authority to determine whether or not to destroy or quarantine infected animals, in other words, it is perfectly discretionary with him; and in our own particular case the inspector who was a witness at the trial testified that he did not order the animals destroyed. (R. 102.) As a matter of fact, the inspector had not even quarantined them until some months after the sale from the Martins to the Sheelys had taken place. If then, in one part of the statute it is perfectly legal to permit the cows to be left in a herd by the inspector appointed for that purpose and for them to be milked and the milk sold if pasteurized, then the absurdity naturally follows that Section 2 of the Act prohibits one to own, have them in his possession or sell them. The only possible reasonable interpretation of Section 2 would be that the prohibition against owning, having them in one's possession or selling them would be effective if they had been condemned and ordered destroyed by the inspector. It is to be noted that the whole Act, even the penalty provisions of Section 4, are aimed at the transportation of diseased cattle or other animals, and apparently the words with reference to owning, having in one's possession, selling or transferring them were added without due consideration of the main purpose of the Act and the effect which such words would have if taken literally.

(c) It is readily apparent from an examination of the conditional sales agreement Section Sixth (R. 13) and from the testimony (R. 137) that the question of Bang's Disease was very much in the minds of the parties at the time the original contract for the sale was drawn, and that the only chance of the plaintiffs and appellees to get away from the plain wording of their agreement is to try to get under the terms of the foregoing statute. The Sixth Section of the agreement reads as follows: "Sixth: It is understood and expressly agreed that the buyers have inspected the property covered by this agreement and are familiar with the condition thereof and that the same is sold to the buyers without any warranties or representations of any kind or character whatsoever on the part of the sellers, save and except that the sellers warrant and agree that they are the lawful owners thereof and have full right, power and authority to sell and dispose of the same and that there are no existing liens or encumbrances against said property or any part or portion thereof." The appellants therefore warrant the title but in all other respects the appellees were on their notice in purchasing the property and did know the condition at the time of the purchase. The appellants throughout the trial, by way of demurrer, objections to the evidence and motions for nonsuit, continuously raised the issue that the complaint and amended complaint did not state facts sufficient to constitute a cause of action.

It is a rule of law so well settled that there is no necessity of quoting individual cases, that for the

plaintiffs and appellees to recover by way of rescission or cancellation they must on their part, even where there is fraud, offer to do equity themselves. Your attention is directed to the fact that there is no place in the complaint, amended complaint, reply or the testimony, where the plaintiffs and appellees have ever at any time offered to make any restitution to the defendants and appellants—in fact the whole history shows a studied course of conduct on their part which is just the opposite. Months after they had ceased making any payments whatsoever, even by way of rental, they were still operating the business for their own benefit, butchering the cows, particularly when the sales price of beef had increased to a large extent (R. 120) and the price of feed and the difficulty of obtaining help had grown. The conditional sales agreement was made on June 26, 1941, the complaint was verified December 27, 1941, the action was commenced on May 13, 1942, nearly a year after the conditional sales agreement was entered into, and most of the cows were killed in the very end of 1942, in September, October and November, without even consulting appellants, let alone offering to make any return of the property and cattle to them.

The plaintiffs and appellees in this case have apparently been taking the position throughout that these particular cattle that might have had Bang's Disease were practically the sole item covered by this transaction; but it takes only a cursory examination of the papers which are attached to the complaint and answer as exhibits to find that the cattle were only a

part of the transaction. They were actually purchasing a going business which had been in existence for years, a large number of items of personal property in addition to the cattle, together with a lease on an extensive tract of land, and there is not even an intimation that any of these other items were not lawful items of commerce. The court's attention is drawn to the case of *Hermanos v. Matos,* 81 Fed. (2d) p. 930, arising in Puerto Rico. In this case plaintiffs sued in the District Court of San Juan, Puerto Rico. The case involved the purchase from defendants of 122 head of dairy cattle for $18,000.00. After the purchase it was discovered that 43 of the cattle died of tuberculosis, a contagious disease, and after further tubercular test was made it was found that 29 more were affected with tuberculosis which had been contracted prior to the sale and that the plaintiffs were ready and willing to return to the defendants, and offered so to do, all the surviving cattle. This offer the defendants refused and plaintiff, after such tender, sued for the entire purchase price. The District Court held that there was a failure of consideration and that plaintiff recover the full purchase price and defendant take back the remaining sound cattle. The Supreme Court of Puerto Rico on appeal held that plaintiff's action did not rest on failure of consideration but was redhibitory in character and was subject to the forty-day rule of that territory, namely, within which period of time such an action could be maintained. The District Court had held that there could be no valid sale of diseased cattle. The Supreme Court of

Puerto Rico, 46 Puerto Rico Rep. 454, however held the sale valid of diseased cattle which plaintiff was seeking to rescind and that the action was redhibitory. The court said that the case depended upon the true construction of Section 1397 of the Puerto Rico Civil Code which reads as follows:

> "Animals and cattle suffering from contagious diseases shall not be the subject of a contract of sale. Any contract made with regard to the same shall be void."

The Supreme Court of Puerto Rico further held that this section did not make contracts for the sale of tubercular cattle void but voidable subject to the rescission at the option of the vendee, and if the vendee elected to rescind he must return to vendor the tubercular cattle and that the action was redhibitory and barred by Section 1399 of the Puerto Rico Civil Code which reads as follows:

> "Redhibitory action, based upon the vices or defects of animals must be instituted within 40 days, counted from their delivery to the vendee, unless, by reason of the customs in each locality, longer or shorter periods are established.
>
> "This action in the sale of animals may only be enforced with regard to the vices and defects of the same, determined by law or by local customs."

After decision by the Supreme Court of Puerto Rico dismissing plaintiff's redhibitory action for rescission by reason of its not having been brought within the forty-day period as provided by statute, the case was

appealed to the United States Circuit Court of Appeals, First Circuit, and was heard before Bingham and Morton, Circuit Judges, and Morris, District Judge. The court stated that the penal and other provisions of the statute form a plan for dealing with the menace to public health occasioned by diseased animals; that Section 1397 is part of this plan and should be so considered. The Circuit Court further points out the reasoning of the Supreme Court of Puerto Rico and holds that the unitary character of a herd of cattle is not applicable but individual animals only. The Circuit Court of Appeals reversed the Supreme Court of Puerto Rico and ordered the cause back to the District Court of San Juan with leave to plaintiffs to amend their complaint after the Supreme Court had dismissed the complaint. Thereafter certiorari was taken to the Supreme Court of the United States, *Matos v. Hermanos,* and that court reversed the Circuit Court of Appeals and affirmed the judgment of the Supreme Court of Puerto Rico. This opinion is set forth in 300 U. S., p. 429.

Thereafter a petition for rehearing was made to and denied by the Supreme Court of the United States April 26, 1937. 301 U. S. 712.

The Circuit Court of Appeals in its opinion, 81 Fed. (2d) 930, discusses the opinion of the Supreme Court of Puerto Rico and has this to say (p. 931):

> "The Supreme Court held that there had been a valid sale of the diseased cattle which the plaintiffs were seeking to rescind and that the action was redhibitory."

(p. 933):

"If the herd of cattle which were sold be regarded as a unit and as the thing which was sold, a different result would be reached because about fifty of the cattle were sound and were legitimate objects of sale. The thing sold was not therefore completely unlawful as an object of commerce; the good portion of it would pass to the vendee and would have to be returned by him if he elected to rescind; the action would be redhibitory in character and would be limited by the provisions of section 1399. The Supreme Court of Puerto Rico did not, however, so regard the transaction. It said: 'We have the idea that when cattle are sold, even for a dairy, the animals are sold individually. It is a distributive sale. It makes no difference that the sale was for a lump sum. With the exceptions noted in the chapter, only the cattle affected with a redhibitory vice' (the Supreme Court regarded tuberculosis as being of that character) 'under all the codes and the commentators that we have seen, may be returned. * * * *The defendant had a clear right to insist that the contract was good for the cattle that were sound.* * * * Before concluding this opinion we desire to say, and this appears possibly from our general considerations, that *the plaintiffs never had the right to the cancellation of the whole contract, but only to bring a redhibitory action for the animals that were suffering from or died of* a contagious disease.' (Italics supplied.)"

It is to be noted that Puerto Rico had a specific statute which said that such tubercular cattle could not be the subject of contract and there is no such

statute in Alaska. It is also to be noted that the plaintiffs in that case had made an actual offer to restore cattle to the defendants.

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2. THROUGHOUT THE ENTIRE TRIAL THE DEFENDANTS AND APPELLANTS REPEATEDLY WERE TRYING TO ASCERTAIN WHAT TYPE OF ACTION WAS BEING BROUGHT BY THE PLAINTIFFS AND APPELLEES BUT THEY APPARENTLY DID NOT KNOW THEMSELVES. THE AMENDED COMPLAINT AND REPLY WERE NOT FILED UNTIL THREE DAYS AFTER THE TRIAL HAD BEEN COMMENCED.

The contracts and agreements on their face show that plaintiff and appellee Ross L. Sheely was not a party to them, notwithstanding which, over the objection of the defendants and appellants, the court permitted testimony as to a copartnership by Sheely (R. 83), moneys expended by Sheely (R. 84-85) and testimony by the other members of the Sheely family as to a copartnership. (R. 84-86.)

The court refused to permit defendants and appellants to introduce any testimony relative to the value of the increase of the herd obtained by the plaintiffs and appellees through the sale of calves or the sale of milk or through calves taken to their other ranch at Palmer, Alaska. (R. 122.) In other words, the court took an entirely inconsistent position in saying that the Sheelys should account for a portion of the value of the butchered cows but not for calves or milk.

So too, contrary to the written terms of the lease, defendant and appellee Ross L. Sheely was permitted

to vary the terms thereof by testifying over objection as to what he thought a reasonable rental value of the land, barns and dwelling house might be. (R. 123-124.)

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3. IT IS THE CONTENTION OF APPELLANTS THAT FAR FROM DOING EQUITY, THE DECISION IN THIS CASE IF IT WERE PERMITTED TO STAND WOULD RESULT IN ABOUT AS INEQUITABLE A TRANSACTION AS IT IS POSSIBLE TO IMAGINE.

Appellee Ross L. Sheely had for a number of years been head of the Farm Extension Service of the University of Alaska; was the general manager of the corporation set up by the government to establish the Matanuska farm colony; had for several years operated a farm of his own at Palmer, Alaska, a short distance from Anchorage, Alaska, where he dealt with dairy cattle and sold milk through the Matanuska Cooperative Association, and particularly in view of the provisions of Section Sixth of the conditional sales agreement quoted above it is inconceivable that he would or did not enter into a transaction of this much importance without being thoroughly conversant with all of the circumstances and conditions.

He acquired a going and successful dairy business and after meeting payments only from June until December 1941 he continued to keep said business and all of the property, including cows, personal property, farm land and buildings, for almost a year thereafter without ever returning or offering to return any part thereof to the appellants or to account for any part

or portion of the profits that he derived therefrom. It is undoubtedly true that appellee Ross L. Sheely, rather than his family, was the principal one engaged in the business, notwithstanding the fact that the original contract was drawn at his request with the other members of the family because he was afraid that his obligations to the Matanuska Coop. would interfere. It is also apparent from his testimony (R. 127-128) that he finally started having trouble long after he had made the agreements with the Martins, in getting help, hay, supplies, and that war conditions generally were making it a little difficult for him to continue to operate, notwithstanding all of which it is the appellants' contention that they were unduly restricted by the court in not being permitted to show that he had made a substantial profit through the sale of milk and other products.

We are likewise frank to admit that it is difficult for us to place credence upon his testimony (R. 128-129) that he did not know whether it was possible to determine whether a herd had Bang's Disease; that it never entered his head to see whether or not the cows should or had been examined, and his final statement that "Those are things prohibited by law and it took me some time to find that out" is significant, in view of his previous experience and then being engaged in the business, and because of the fact that the conditional sales agreement was specifically rewritten to insert the clause that there was no warranty of condition and that he had examined the herd and other property.

CONCLUSION.

It appears to us that this was a simple business transaction entered into in good faith for the sale of a going business as is—where is, with full knowledge on the part of all parties concerned; that the Territorial statute did not and could not, in view of the fact that the inspector had never ordered any of these cattle destroyed, make them an article of illegal commerce so as to result in an inequitable consequence; that a purchaser would be permitted to take over the business, conduct it for a year and a half, appropriate all of the proceeds to his own use without making any accounting to the seller, and then return a wrecked business and not only not have to complete his payments but be permitted instead to recover back what he had originally paid.

It is earnestly and respectfully submitted that the maxims of equity have not been followed, that the judgment be reversed and that the true principles of equity be applied in this suit.

Dated, Anchorage, Alaska,
June 16, 1944.

THOMAS M. DONOHOE,
JOHN E. MANDERS,
Attorneys for Appellants.

No. 10,665

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

A. T. MARTIN and ALICE M. MARTIN,
Appellants,

vs.

CHARLOTTE L. SHEELY, JOHN H. SHEELY, JOE A. SHEELY and ROSS L. SHEELY, co-partners,
Appellees.

Upon Appeal from the District Court for the Territory of Alaska, Third Division.

BRIEF FOR APPELLEES.

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BRIEF FOR APPELLEES.

JURISDICTIONAL STATEMENT AND STATEMENT OF THE CASE.

While not converting the jurisdictional statement and statement of the case of the appellants, the appellees quote and adopt as a part of this brief the opinion of the trial Court, which accompanied its decision, believing it to present more clearly the issues involved, the evidence adduced, and the law of the case, as follows:

"OPINION

This matter came on for hearing upon the amended complaint filed herein, in which com-

plaint it is alleged that the plaintiffs as co-partners were engaged in the dairy business; and that in connection with said business all the plaintiffs, except the plaintiff Ross L. Sheely, entered into a conditional sales agreement, a copy of which is attached to the complaint and marked Exhibit 'A', a lease, a copy of which is attached to the complaint and marked Exhibit 'B', and a grazing permit, which is also attached to the complaint and marked Exhibit 'C', that each of said instruments was and is an integral part of the transaction. That said sales agreement was for the purchase of the dairy, including the distributing system and all the equipment and cattle connected therewith, a list of which is attached to Exhibit 'A' attached to the complaint for a total purchase price of Twenty-eight Thousand Two Hundred Ninety-four Dollars ($28,294.00), $9800 of which was paid upon the execution of the agreement and $308.22 on the 10th of each and every month thereafter until the purchase price had been fully paid with interest at the rate of 6% per annum from July 1, 1941. That the chief item purchased under said sales agreement was 56 cows and that the defendants warranted that they were the lawful owners of said cows and had full right, power and authority to sell the same. That the plaintiffs aforesaid, relying upon said warranty and representations, entered into said sales agreement, the lease and the grazing permit, and made the original payment under said sales agreement, paid $200 on account of said lease and $110 on account of said grazing permit and entered into possession of said property on July 1, 1941. That the performance of said conditional sales agreement, lease and grazing permit was guaranteed in writ-

ing by the plaintiff Ross L. Sheely, a copy of which writing is attached to the complaint and marked Exhibit 'D'. That the plaintiffs have performed all the conditions of said agreement, lease and grazing permit to the date of the commencement of this action, and in addition to the initial payment above set forth have paid the sum of $1541.10 and $450 interest on the sales agreement, the sum of $1000 on the lease, and have paid certain sums in connection with a truck, $2000 for hay and grain and have purchased equipment and made improvements on the premises at the cost of $2513. That at the time of the execution of the above instruments, a large number of the cows sold to the plaintiffs were diseased and infected with Bang's disease or contagious abortion, which fact was well known to the defendants and unknown to the plaintiffs, and that the defendants sold and delivered said cows to the plaintiffs with an intent to injure the plaintiffs. That the plaintiffs purchased the cattle for a dairy herd and that said herd was of little value for dairy purposes in the condition in which it was sold. That the plaintiffs have suffered damages in the sum of $15,000. And plaintiffs pray first, that the conditional sales agreement, Exhibit 'A' attached to the complaint, be declared illegal and void, second, that the lease Exhibit 'B' attached to the complaint, the grazing permit, Exhibit 'C' attached to the complaint, also be declared void as a part of the same transaction and that the plaintiffs have judgment against the defendants in the sum of $15,000, and for other equitable relief, costs and an injunction.

The defendants in this case have answered the original complaint, and it was stipulated in open

court that said answer might be considered as an answer to the amended complaint and that defendants might if they should desire plead an estoppel. The defendants by their answer deny that there was any segregation of value for the cows or any other item embodied in said conditional sales agreement. Defendants deny that plaintiffs in making said agreement relied upon the representations of the defendants. Deny that the guaranty agreement of Ross L. Sheely was made at the insistence of the defendants and allege that the transfer of the business from the defendants to the plaintiffs was proposed by the said Ross L. Sheely because he did not wish to appear directly as a purchaser. Defendants deny that the plaintiffs have performed the conditions prescribed in the conditional sales agreement, lease and grazing permit to the date herein. Defendants deny that the plaintiffs have purchased additional equipment and made improvements to the sum of $2513 or any other sum. And, the defendants allege that the plaintiffs did not make the payments specifically to be made by condition of the said conditional sales agreement subsequent to the month of December, 1941, and were and are in default by reason of said non-payments. The defendants deny that at the time of the execution of the sales agreement and for a long time prior thereto a large number of the cows sold to the plaintiffs were infected with Bang's disease or contagious abortion and that this fact was well known to the defendants and unknown to the plaintiffs and deny that they were sold to the plaintiffs with an intent to injure the plaintiffs. The defendants admit that the plaintiffs have killed and disposed of the cows mentioned in the

complaint, but deny that the same were killed or disposed of by necessity and because of said disease. Defendants deny that said herd was infected and deny that said herd was of little value for dairy purposes. Defendants deny that the plaintiffs have suffered damage by any acts or omissions of the defendants, deny that the plaintiffs will suffer irreparable damages if required to perform the agreements, deny that the plaintiffs have no remedy at law and deny that the plaintiffs have suffered damage in the sum of $10,000 or any other sum.

And by way of first counterclaim and first cross-complaint, the defendants allege that the parties entered into the conditional sales agreement, marked Exhibit 'A' attached to the complaint, that the plaintiffs complied with the said agreement during the year 1941, that said agreement was guaranteed by the plaintiff Ross L. Sheely, in writing, Exhibit 'D' attached to the complaint, that the plaintiffs have defaulted on said agreement, that the defendants declare the balance due on said agreement and that is $16,952.90 together with interest at the rate of 6% per annum from December 10th, 1941.

And for second counterclaim and second cross-complaint the defendants allege the execution of the lease agreement, Exhibit 'B' attached to the complaint, that the plaintiff Ross L. Sheely guaranteed the payments therein in writing, Exhibit 'D' attached to the complaint, and that no payments have been made since January, 1942, that the plaintiffs have defaulted and that there is $2000 together with interest at the rate of 6% per annum on each monthly payment of $200 due

and owing thereon and that the defendants are entitled to the immediate possession of the leased premises.

And for a third counterclaim and third cross-complaint, it is alleged that the parties entered into the grazing permit, Exhibit 'C' attached to the complaint; that the sum of $110 was due the defendants on said permit on the 19th day of August, 1942, and that plaintiffs have failed to make said payment and that the defendants are entitled to the immediate possession of the premises described therein. Whereupon, the defendants pray that the plaintiffs' complaint be dismissed, that they have judgment on their first counterclaim in the sum of $16,952.90 together with interest; that they have judgment on their second counterclaim in the sum of $2000, together with interest; and that the defendants have judgment for immediate possession of the premises and property mentioned in defendants' third counterclaim and for costs.

By reply, the plaintiffs state that during all the times in the pleadings referred to plaintiffs were co-partners; that the contracts set forth, Exhibits 'A', 'B', and 'C' attached to the complaint were entered into by the parties thereto for and in behalf of all the plaintiffs. And, replying to the affirmative defenses in addition to certain allegatons previously made, state that the chief item contained in the property purchased under Exhibit 'A' attached to the complaint, was 56 head of cows which were figured at $300 per head; the plaintiffs repeat the allegations as to the sums of money paid; allege that the cattle were diseased and infected and make the same allegations as to the defendants' second and third counterclaims.

This cause came on for hearing before a jury on Monday, the 21st day of December, 1942, at which time evidence was offered by the plaintiffs to the effect that the herd of cattle owned by the defendants was examined in April, 1941, by Earl F. Graves, a veterinarian employed by the Territory of Alaska for the purpose of testing cattle for Bang's disease and other diseases; that on the 22nd day of April such examination was made at which time there were 21 cattle of said herd definitely infected with Bang's disease and 8 were suspects; that after making said tests the said veterinarian notified the defendant A. T. Martin of the result of said tests, made re-tests in the presence of said Martin and thereafter fully informed the said A. T. Martin of the condition of his herd; at which time the said Graves gave said Martin a copy of his report, marked Plaintiffs' Exhibit 'A' in this cause. That in June, 1941, negotiations were entered into between the plaintiffs and the defendants which resulted in the agreements being entered into, Plaintiffs' Exhibits 'A', 'B', 'C' and 'D' attached to the complaint herein. That the payments alleged to have been made in the complaint were thereupon made and the plaintiffs went into possession of said herd. That prior to the execution of said agreement the defendant A. T. Martin claims that while the plaintiff Ross L. Sheely was at the premises transferred he informed him that there was some Bang's disease in the herd, this is denied by the plaintiff Sheely. That in connection with the execution of the conditional sales agreement, Plaintiffs' Exhibit 'A' attached to the complaint and while discussing the clause under which defendants claim they sold this herd without any warranties what-

soever, the plaintiff Sheely testified that the following conversation was had:

Mr. Donohoe. Do you recall in my office, you being present, your family being present, Mr. Martin being present, Mr. Cuddy being present and myself, discussing the clause in the contract of no warranties and there was a discussion regarding to your having inspected the cows, knowing their condition and that there was no guarantee on it?

Mr. Sheely. Yes.

Mr. Donohoe. There was such a discussion at the time?

Mr. Sheely. May I say what the discussion was?

Mr. Donohoe. Yes.

Mr. Sheely. We were in your office, Mr. Donohoe, I was there and Mrs. Sheely, Jack was there, Joe was there, Mr. and Mrs. Martin were there, yourself and Mr. Cuddy. Mr. Cuddy said what about Bang's disease. Mr. Martin said I don't know anything about it, but he did know about it. He knew it was against the law to sell diseased cows. All he said was there was no warranty in the contract.

Mr. Donohoe. Didn't Mr. Martin tell you it was impossible to determine whether or not there was Bang's disease in these cows?

Mr. Sheely. He said there was no warranty as to the health of the cows. He did not tell me whether it was possible to determine whether they had Bang's disease.

Nowhere in the evidence is it claimed that the defendant made full disclosures of the condition of the herd. That sometime after the herd was

delivered to the plaintiffs one of the cows of the said herd aborted, but that the plaintiffs paid little attention to the same for the reason that it is not infrequent that abortions occur. That thereafter and sometime in September, while the plaintiffs had taken some of the purchased cows to their ranch at Palmer, they were informed by the Health Department that a restriction had been put on said herd on account of Bang's disease and that plaintiffs were not allowed to move said cattle. That during the fall of 1941 several more of the cows aborted; that the plaintiffs made improvements on the premises as shown by Plaintiffs' Exhibit 'D'; that the plaintiffs slaughtered several of the cattle; that thereafter and in January, 1942, the witness Graves made another examination of the herd at which time he found that 32 of the remaining herd were infected with Bang's disease, 8 were clean and the balance were suspects. That thereupon the plaintiffs brought this action.

The evidence shows that of the original herd purchased 36 were slaughtered and sold for beef for which the plaintiffs derived $4472.20, six died and that there are 14 cows and one bull left of the original herd. That the plaintiffs brought 13 cows and one bull from Palmer which are now on the premises, that 8 or 9 of these cattle were brought from Palmer before the plaintiffs had full knowledge as to the diseased condition of this herd, but plaintiffs had some knowledge thereof and that the balance were brought to the premises from Palmer after the plaintiffs were fully informed of the diseased condition of the herd. That the plaintiffs paid the defendants under Exhibit 'A'

attached to the complaint the sums of $9800, $1541.10 and $450 interest; that the plaintiffs paid the defendnats under Exhibit 'B' attached to the complaint the sum of $1200, and the sum of $110 under Exhibit 'C' attached to the complaint; that the plaintiffs paid to the defendants either directly or indirectly for feed the sum of $2000, and have paid for improvements the various items stated in Plaintiffs' Exhibit 'D' only part of which has been delivered. The evidence also shows that the plaintiffs have paid defendants an indefinite amount in connection with the purchase of trucks but since these trucks were afterwards disposed of by the plaintiffs this amount becomes immaterial. The plaintiff Ross L. Sheely testified that the reasonable rental value of the premises under the circumstances was $50 per month. The plaintiffs stipulated that their complaint and the defendants that their counterclaims are in equity. Whereupon, the Court dismissed the jury.

Chapter 55, *Alaska Session Laws,* 1919, provides as follows:

'Section 1. To import or to bring, into the Territory of Alaska, animals of whatsoever kind or character, diseased or infected with the diseases mentioned in Section 3 of this Act, is hereby declared to be injurious to the public health, against public policy, illegal, and punishable as herein provided.

Section 2. To own, have in one's possession, sell, transfer, transport, drive or convey from one section of the Territory to another, animals or livestock of whatsoever kind or character, diseased or infected with the diseases mentioned in Section 3 of this Act, is hereby declared to

be injurious to the public health, against public policy, illegal, and punishable as herein provided.

Section 3. It shall be unlawful to bring, into the Territory of Alaska, any horses, cattle, or swine, for work, feeding, breeding or dairy purposes, without first having such animals examined and found free from the following contagious diseases: glanders, farcy, tuberculosis, actinomycosis, rinderpest, foot and mouth disease, contagious abortion, contagious keratitis, scabies, maladie du coit, swine plague and hog cholera, * * *

Section 4. For each evasion or violation of any provision of the three sections last preceding, the shipper or party responsible for the evasion or violation, shall be fined not more than Five Hundred Dollars ($500.00); * * *'

6 *R. C. L., Contracts,* p. 701, Sec. 107:

'Express or Implied Prohibition.—A contract directly and explicitly prohibited by a constitutional statute in unmistakable language is absolutely void. That has never been judicially doubted, and is unanimously conceded. To hold such a contract binding would be to enforce that which the legislature has forbidden, to give effect to that which the legislature has declared void,—the repeal of a law by judicial construction. However, it is not necessary that there should be an express prohibition in a statute to render void a contract made in violation of it.

108. Implication from Imposition of Penalty.—In order that there may be an implied prohibition the imposition of a penalty is not essential.

In other words, it is not necessary that a statute should impose a penalty for doing or omitting to do something in order to make void a contract which is opposed to its operation. The obverse of this proposition is, however, the basis of a well established rule, which dates at least from the time of Lord Holt. The rule, as stated in the early decisions, is that every contract made by or about a matter or thing which is prohibited and made unlawful by any statute, is a void contract, though the statute itself doth not mention that it shall be so, but only inflicts a penalty on the offender, because a penalty implies a prohibition though there are no prohibitory words in the statute. Although it might perhaps not warrant the conclusion that a penalty implies a prohibition for the purpose of making the offense punishable by indictment in case the law had prescribed another and a specific punishment for the offense, Lord Holt's remark is an authority for the proposition that a contract made in direct violation of a statute providing a penalty for the violation thereof is illegal though the contract is not in express terms prohibited or pronounced void.'

Restatement of the Law, Contracts, p. 1109:

'Topic 12. Effect of Illegality. Sec. 598. Generally No Remedy on an Illegal Bargain. A party to an illegal bargain can neither recover damages for breach thereof nor, by rescinding the bargain, recover the performance that he has rendered thereunder or its value, except as stated in Secs. 599-609.

Comments:

a. The statement that all illegal bargains are void is not wholly accurate. It is true that many such bargains are entirely without effect on the legal relations of the parties and that a court will only under very exceptional circumstances enforce specifically an illegal agreement, but the rule of public policy that forbids an action for damages for breach of such an agreement is not based on the impropriety of compelling the defendant to pay the damages. That in itself would generally be a desirable thing. When relief is denied it is because the plaintiff is a wrongdoer, and to such a person the law denies relief. Courts do not wish to aid a man who founds his cause of action upon his own immoral or illegal act. If from the plaintiff's own statement or otherwise it appears that the bargain forming the basis of the action is opposed to public policy or transgresses statutory prohibitions, the courts ordinarily give him no assistance. The court's refusal is not for the sake of the defendant, but because it will not aid such a plaintiff. So if the plaintiff and defendant changed sides, and the defendant, equally in fault, was to bring his action against the plaintiff, the latter would then have the advantage; for where both are equally in fault the position of the defendant is the stronger.

b. To deny such persons recovery, though an equally guilty defendant thereby escapes punishment, tends to diminish the number of illegal agreements. But not all illegal agreements are for that reason void. A rule to that effect would have unfortunate consequences, since in many

cases it would protect a guilty defendant from paying damages to an innocent plaintiff, or would otherwise produce undesirable results. Cases of this sort are covered by the rules stated in Secs. 599.608. Doubtless a statute can and sometimes does make a bargain absolutely void, but even though a statute so states in terms, "void" sometimes means voidable, and unless no other conclusion is possible from the words of a statute, or from the policy on which a statute is based, it should not be held to make all agreements contravening it wholly void.

c. The rule stated in the Section precludes recovery on principles of quasi-contract for benefits conferred under an illegal bargain, as well as an action on the bargain itself.

Sec. 599. Ignorance of Facts Rendering Bargain Illegal. Where the illegality of a bargain is due to

(a) facts of which one party is justifiably ignorant and the other party is not, or

(b) statutory or executive regulations of a minor character relating to a particular business which are unknown to one party, who is justified in assuming special knowledge by the other party of the requirements of the law

the illegality does not preclude recovery by the ignorant party of compensation for any performance rendered while he is still justifiably ignorant or for losses incurred or gains prevented by non-performance of the bargain.'

Restatement of the Law, Restitution, p. 595:

'Sec. 149. * * * Actions for restitution have for their primary purpose taking from the defendant and restoring to the plaintiff something to which the plaintiff is entitled, or if this is not done, causing the defendant to pay the plaintiff an amount which will restore the plaintiff to the position in which he was before the defendant received the benefit. If the value of what was received and what was lost were always equal, there would be no substantial problem as to the amount of recovery, since actions of restitution are not punitive. In fact, however, the plaintiff frequently has lost more than the defendant has gained, and sometimes the defendant has gained more than the plaintiff has lost.

In such cases the measure of restitution is determined with reference to the tortiousness of the defendant's conduct or the negligence or other fault of one or both of the parties in creating the situation giving rise to the right to restitution. If the defendant was tortious in his acquisition of the benefit he is required to pay for what the other has lost although that is more than the recipient benefited. If he was consciously tortious in acquiring the benefit, he is also deprived of any profit derived from his subsequent dealing with it. If he was no more at fault than the claimant, he is not required to pay for losses in excess of benefit received by him and he is permitted to retain gains which result from his dealing with the property. There are situations not falling within the above categories as to which, while they are subject to the

general equitable principle that restitution is granted to the extent and only to the extent that justice between the parties requires, it is not feasible to make specific statements (see the Caveat to Sec. 155).'

Under the law and the evidence above cited, there can be no question but what the contracts involved in this case are illegal and should be declared so. This disposes of the defendants' counterclaims because there can be no breach of these illegal contracts for which the defendants can recover. Under the evidence the Court must find that the defendants had full knowledge of the facts making this contract illegal, and further that the defendants did not make full disclosure of said facts before entering into this contract. There was some talk of Bang's disease when the parties were about to enter into these contracts, at which time the clause of the contract relieving the defendants from warranties was discussed. And, the defendant A. T. Martin claims that he discussed the matter with the plaintiff Ross L. Sheely, which the plaintiff Ross L. Sheely denies, but at no time does said defendant or either of them claim to have made full disclosures. This, taken in connection with the allegations of the answer herein, wherein the defendants specifically deny that they had knowledge of the fact that the herd was infected with Bang's disease previous to entering into the contract, leaves the Court to find that the defendants purposely and deliberately kept these facts from the plaintiff, and that, therefore, the plaintiffs were ignorant of the facts which made the contracts illegal, and for that reason are entitled to recover the moneys paid under the contracts since the Court finds that these

contracts although executed separately are all part of the illegal transaction. Therefore, the Court finds that the plaintiffs should recover from the defendants the sum of $9800, $1541.10 and $450 interest, moneys paid under the contract Exhibit 'A' attached to the complaint, $1200, moneys paid under Exhibit 'B' attached to the complaint, $110 paid under Exhibit 'C' attached to the complaint, $1766.85 paid under Exhibit 'D' attached to the complaint, which is the full amount delivered under said exhibit, but does not include supplies on order, which are the plaintiffs and which the plaintiffs are allowed to divert and dispose of in whatever manner they see fit, except that the Court excludes from the items set up in that exhibit, $32.50 paid for supplies, milk cases, etc., $110.90 paid for quart bottles, and $80 paid for one-half pint bottles, for the reason that it is not shown by the evidence that these supplies purchased in connection with the running of said business are in excess of the inventory attached to the complaint. The Court also deducts 50% of the three items mentioned in said exhibit, milk pump motor—$17.50, separator motor—$40 and a Crepaco electric motor for milk pump—$17.50, and the amount paid for painting the milk room—$6.00, making a total of $14,867.95 with interest on the various amounts from the time they were incurred, less $4472.20, which the plaintiffs received for the slaughtered cattle, and since the dates this sum was received does not appear in the record no interest can be allowed on same.

The Court disallows the plaintiffs the claim for $2000 for hay purchased at the time the original contracts 'A', 'B' and 'C' attached to the complaint were entered into or shortly thereafter, be-

cause the Court finds that said transaction was collaterally connected with the illegal bargain only.

Restatement of the Law, Contracts, p. 1108:

> 'Sec. 597. Bargain Connected Collaterally With Illegality. A bargain collaterally and remotely connected with an illegal purpose or act is not rendered illegal thereby if proof of the bargain can be made without relying upon the illegal transaction.'

The Court finds that the cattle delivered by the defendants to the plaintiffs are accounted for by the cattle still remaining on hand, those slaughtered and those that have died, and that therefore the cattle delivered have been fully accounted for. The Court finds that the plaintiffs brought certain cattle to the premises of which the plaintiffs took possession at the time the illegal contracts were executed, that these cattle are still the cattle of the plaintiffs to be disposed of as the plaintiffs see fit, either by slaughtering or removing them if that is possible. The Court feels that under the evidence in this case, part of said cattle were brought to the premises after the plaintiffs had full knowledge of the facts and clearly the plaintiffs would not be entitled to recover from the defendants for such cattle; that part of the remaining cattle were brought there when the plaintiffs had considerable knowledge of the facts and would be required to investigate further before bringing cattle there for which they could hold the defendants liable. The first of these cattle were, however, brought there when the plaintiffs had no knowledge or very little knowledge of said disease. If the Court made the defendants pay

$300 apiece for these cattle as it is contended for by the plaintiffs, the Court would in fact be making and enforcing an illegal transaction. Under the circumstances, the Court is going to offset whatever the plaintiffs were entitled to under said claim against whatever claim the defendants may be entitled to for rent of the premises, which right seems very doubtful to the Court because the rent is part of and closely connected with the illegal contracts.

It will be noted that the plaintiffs under the above opinion will recover less than they would be able to retain if the Court had found that the parties were in pari delicto as well as particeps criminis and left them where they placed themselves, without giving aid to either party. If this had been done the plaintiffs would have been entitled to retain $12,000 worth of personal property, the $4472.20 obtained for the cattle that were slaughtered and the cattle on the ranch. The plaintiffs, however, will have the satisfaction of knowing that what they have obtained in this case was by virtue of the principles of equity and good conscience and not merely by being in an advantageous position under an illegal contract in which they were in pari delicto.

The plaintiffs may prepare findings of fact, conclusions of law, and a decree in accordance with this opinion.

Dated at Anchorage, Alaska, this 30th day of December, 1942.

Simon Hellenthal,
District Judge."

ARGUMENT.

CONSTITUTIONALITY OF ACT.

Appellants contend that Section 2 of Chapter 55, Session Laws of Alaska, 1919, is unconstitutional and void as being in conflict with the Organic Act of Alaska which provides:

> "No law shall embrace more than one subject, which shall be expressed in its title."

The title to the Act in question and Section 2 thereof are set forth in full on page 19 of appellants' brief:

The constitutional provision under discussion is a provision common to the constitutions of most if not all of the states. In all text books on the question, the object and purpose of such provisions is first discussed. Following this precedent we submit the following:

> "The purposes of these constitutional provisions have been summarized as follows:
>
> (1) To prevent 'log-rolling' legislation.
>
> (2) To prevent surprise, or fraud, in the legislature by means of provisions in bills of which the title gives no intimation.
>
> (3) To apprise the people of the subject of legislation under consideration."

Citing

> Ruling Case Law, Vol. 25, Sec. 83, Cooley's Constitutional Limitations.
>
> "These provisions are intended to prevent the evils of 'omnibus bills', and surreptitious legislation."

"Log-rolling" is an expression of such well known significance as to probably not require definition. It is sufficient to cite the following from the Juneau Empire of September 8, 1942:

> "Q. What does the political term 'log-rolling' mean?
>
> A. When congressmen get other members to vote for something beneficial to their own districts, in exchange for similar courtesies."

It is evident that the constitutional provision in question has none of the ear-marks of surreptitious, log-rolling or fraudulent legislation. So that the objections of defendant to the Act become, at least, technical.

Attention having been called to the evils, to remedy which the constitutional provision has been adopted, it is next in order to discuss the consequent rules of construction of such statutes, which the authorities unanimously approve.

> "THE PROVISIONS OF THE VARIOUS CONSTITUTIONS RELATING TO the subject-matter and titles of acts should be construed liberally to uphold proper legislation, all parts of which are reasonably germane, on the one hand, and to prevent trickery on the other hand. The restriction requiring the subject of an act to be expressed in its title should be reasonably construed, considering substance rather than form, to require the expression in the title of the general object *but not the details or incidents, or means of effecting the object sought.*"
>
> 16 *Cyc.*, page 1017.

"CANONS OF CONSTRUCTION have been adopted which may be summarized as follows: *That every law is presumed to be valid;* that this provision of the constitution is to be liberally construed and *all doubts resolved in favor of the law;* that the title should also be liberally construed giving to its general words paramount weight; that it is not essential that the best or even accurate words in the title be employed, but the remedy to be secured and mischief avoided furnish the best test of its sufficiency to prevent such title from being made a cloak or artifice to distract attention from the substance of the act, *provided the title be fairly suggestive,* and not foreign to the purpose of the statute."

State v. State Institutions Board of Control, 88 N.W. 533.

In *Blair v. Chicago,* Justice Day speaking for the Court says:

"The Illinois cases were reviewed and the conclusion reached that the purpose of the constitutional provision is reached if the title is comprehensive enough as reasonably to include within the general subject or the *subordinate branches thereof,* the several objects which the statute seeks to effect. And it was held that generality of the title is no objection to a law so long as it is not made to cover legislation incongruous in itself, and which by no fair intendment can be included as having necessary or proper connection. * * * The Montclair Twp. Case held I. That this provision does not require the title to the act to set forth a detailed statement or an index or abstract of its contents; nor does it prevent uniting in the

same act numerous provisions having one general object, fairly indicated by its title. * * * Now, the object may be very comprehensive and still be without objection, and the one before us is of that character, but it is by no means essential that every end and means necessary or convenient for the accomplishment of the general object should be either referred to or *necessarily indicated by the title.*"

Blair v. Chicago, 201 U.S. 452.

"The history and object of this constitutional provision, and the mischief against which it was aimed, should be kept steadily in view by the courts in its construction and application. It was intended to prevent the practice common in legislative bodies not thus restricted of embracing in the bill matters having no relation to each other, wholly incongruous, and of which the title gives no notice, thus securing the adoption of measures by fraud, and without attracting attention, or combining subjects representing diverse interests, in order to unite the members who favored either in support of all. These combinations, being corruptive of the legislature and dangerous to the state, are prohibited in most if not all the states by constitutional provisions. This provision of the constitution was not designed to embarrass legislation, but to put an end to legislation of the vicious character referred to, and has been always liberally construed to sustain legislation not within the mischief. * * * A disregard of the constitutional provision will be fatal, but the departure must be plain and manifest, and *all doubts will be resolved in favor of the law.*

The conflict between the constitution and the law should be palpable and clear before the courts should disregard a legislative enactment upon the sole ground that it embraces more than one subject. (Sutherland St. & Const. Law Sec. 82.)

If all the provisions of the law relate directly *or indirectly* to the same subject, are naturally connected and are not foreign to the subject expressed in the title, they will not be held unconstitutional as in violation of this clause of the constitution."

State v. Shaw, 29 Pac. 1028 (Ore.), citing:
O'Keefe v. Weber, 14 Ore. 55;
Bowan v. Cockril, 6 Kan. 311;
Gillitt v. McCarthy, 25 N.W. 637.

"An act, no matter how comprehensive, would be valid provided a single main purpose was held in view, and nothing embraced in the act except what was naturally connected with and incidental to that purpose."

Van Horn v. State.

"Penal provisions are not repugnant to the constitutional provisions."

36 *Cyc.,* page 1023.

In conclusion, under this head, the object or purpose of the Act is the eradication of diseased cattle now in the Territory of Alaska. Section 2 of the Act provides one of the means to that end. It is germane to the subject and object. The title is "suggestive of" and not foreign to the purpose of the statute.

After a voluminous argument and citation of authorities to support the contention that the Act in question is illegal, appellants advanced the proposition (page 29 (b) appellants' brief) that the Court write into the statute the words:

"After inspection and quarantine or destruction ordered" so as to make it read,

> "*After inspection and quarantine or destruction ordered,* to own, have in one's possession, sell, transport, drive * * * animals or livestock * * * diseased or infected is declared hereby to be injurious to the public health, against public policy, illegal and punishable, as hereinafter provided."

In other words the gist of the offense is "getting caught", which is a popular idea among certain classes. No matter how purposely, nor with what evasive methods, nor with what guilty knowledge the law might be violated, it is contended that no crime has been committed, until after inspection etc. ordered, and a subsequent defiance of the law.

Appellants contend that the necessary provisions of the Act in question regarding the disposition, quarantine or destruction of diseased cattle and other regulations, common to all such legislation, qualify and virtually nullify the plain provision of the law prohibiting and illegalizing the sale of diseased cattle. Such a construction would necessarily defeat the purpose of the Act. The aforesaid provisions for the disposition of diseased animals by destruction or quarantine stand by themselves and are not to be

construed as legalizing contracts of sale or repealing penal provisions.

THE CONTRACT OF SALE WAS ILLEGAL AND VOID.

There are three principles of law which affect the rights to the parties to this action, and which are established unanimously by the authorities.

First: A contract expressly prohibited by a valid statute is void. This proposition has no exception, for the law cannot at the same time prohibit a contract and enforce it.

McManus v. Fulton, 67 A.L.R. 696.

A contract directly and explicitly prohibited by a constitutional statute in unmistakable terms is absolutely void. That has never been judicially doubted and is unanimously conceded.

6 *Ruling Case Law,* 701.

Second: It is also well established that money paid on a void contract made in violation of statutory provision where the parties are *in pari delicto,* and *particeps criminis,* cannot be recovered; that the law will not lend its aid to either party, but will leave them where they have placed themselves.

The above principle is conceded by the plaintiffs and needs no authority.

Third: The converse of the second principle above stated is also true. Equity will lend relief where

parties to an illegal contract are not *in pari delicto,* and aid the one comparatively more innocent.

Marshall v. Lovell, 19 F. (2d) 751, and certiorari in 276 U.S. 616.

The overwhelming evidence in this case is that the parties are not *in pari delicto;* that the defendants well knew the condition of the cattle sold to the plaintiffs at the time of said sale, and deliberately concealed their condition as to their being inflicted with contagious abortion, and failed to disclose to plaintiffs the report on tests of said cattle made by the Territorial Veterinarian.

The most extreme view of the testimony against the plaintiffs only shows grounds for a suspicion on their part of the existence of contagious abortion in the cattle purchased, while the undisputed evidence shows that the defendants knew they were infected. In this respect the case at bar is on all fours with the case of

Groves v. Jones, reported in the 233rd N.W. page 375 (a contagious abortion case).

In that case the only evidence produced to show the diseased condition of the cattle was the test report which was introduced by the defendant, and therefore held binding on him. In the case at bar the test reports were introduced by the plaintiffs, but the Territorial Veterinarian himself was on the witness stand and gave direct evidence of the blood tests and condition of the cattle.

The last case above cited also establishes the right of plaintiffs to recover back that part of the purchase price paid, citing 6 *Ruling Case Law,* page 833, as follows:

> "A distinction has been made between those illegal contracts, both parties to which are equally culpable and those in which, although both have participated in the illegal act, the guilt rests chiefly on one. Unless therefore, the parties are *in pari delicto* as well as *particeps criminis,* the courts, although the contract is illegal, will afford relief where equity requires it to the more innocent party even after the contract has been executed."

See also,

Skinn v. Reutter, 97 N.W. 152,

in which the purchaser of diseased hogs, who placed them with his own hogs, causing their death, was entitled to recover the purchase price of the hogs purchased, together with the value of his own hogs.

Also,

> "when seller knows of the presence of the disease, he is liable for all direct and consequential damages resulting therefrom, if he fraudulently fails to communicate his knowledge to purchaser."
>
> *Cheeseman v. Felt,* 142 Pac. 285.

Appellants throughout their brief, as in fact was the case throughout the trial, stress paragraph six of the Conditional Sales Agreement, as barring recovery by plaintiffs. The paragraph is as follows:

> It is understood and expressly agreed that the buyers have inspected the property covered by this agreement and are familiar with the condition thereof, and that the same is sold to the buyers without any warranties or representations of any kind or character whatsoever on the part of the sellers, save and except that the sellers warrant and agree that they are the lawful owners thereof and have full right, power and authority to sell and dispose of the same and that there are no existing liens or encumbrances against said property or any part or portion thereof.

Appellants ignore the principle of law unanimously conceded by all authorities that:

> A party to an illegal contract cannot, either at the time of the execution of the contract or afterward, waive his right to set up the defense of illegality in any action thereon by the other party.
>
> 13 *Corpus Juris,* Section 451 and cases cited.

> "The defect cannot be gotten rid of either by failure to plead it, or by agreement to waive it in the most solemn manner. The law will not enforce contracts founded in its violation."
>
> *Levy v. Davis,* 80 L. Ed. 791.

THE PARTIES WERE NOT IN PARI DELICTO.

There is overwhelming evidence to sustain the finding of the trial Court that the parties were not *in pari delicto.* It is true that in the testimony of Martin,

appellant (R. 138-139), there is the positive statement that Martin told Sheely, appellee, with reference to Bang's Disease, "that some were reactors according to the veterinarian." An extract from this testimony (R. 138)is as follows:

> "I told him some were reactors according to the veterinarian. Graves was the veterinarian. He didn't ask me to show it to him. Just he and I were there. No one else was there. No, he didn't ask me to tell him the gist of it. No, I didn't tell him I had the report. I had a copy. No, he didn't ask to see it."

From the above extract it might be inferred that Martin testified that he told Sheely that he had a copy of the veterinarian's report showing Bang's Disease in the herd and that Sheely negligently failed to ask to see it, this from the words:

> "No, I didn't tell him I had the report. I had a copy."

This is an illustration of how a condensation into narrative form can be misleading, if not carefully checked, as was the case in this instance.

Therefore, with apologies to the Court, and as by way of illustration, we go outside the record and insert an extract from the cross-examination of Martin, as follows:

> "By Mr. Grigsby:
>
> Q. When did you say you had this conversation with Mr. Sheely?

A. It was previous to the time of the sale of the herd, when he was inspecting the place.

Q. How long before?

A. Only a few days before the purchase.

Q. The conversation in which he talked about Bang's disease?

A. A very few days before.

Q. You told him you didn't know whether or not they were infected?

A. I told him some were according to the veterinarian's were re-actors.

Q. Which veterinarian?

A. Graves.

Q. Did you show it to him?

A. He didn't ask for it.

Q. Who was there?

A. Just he and I.

Q. No one else there?

A. No, Sir.

Q. Did you tell him the gist of it?

A. No, he didn't ask it.

Q. You told him you had the report?

A. No.

Q. You had a copy?

A. Yes.

Q. He didn't ask to see it?

A. No.

Q. He didn't ask how many were infected or any details at all?

A. No, Sir."

Also, Martin testified (R. 137):

"I did have a conversation with Mr. Sheely prior to his purchase of the place with reference to Bang's Disease. * * * Mr. Sheely asked me out behind the barn. I said I couldn't say the

exact status. I said some was shown a year and a half ago and I had butchered some reactors since then and couldn't state the present status."

Not a word about any veterinarian's report.

This conversation was a few days before the purchase, which was June 26, 1941, and Graves, the Territorial Veterinarian testified:

"On April 22, 1941, I examined the herd of Mr. Martin—no tuberculosis re-actors; I did find 21 contagious abortion and 8 suspect re-actors and the rest were clean. * * * Mr. Morley of the Territorial Board of Health and Mr. Martin and myself were present at the time of the examination. * * * I ran the bloods down in the hotel. * * * I found so many re-actors that I thought Martin should see some of them run. Morley had Martin come up, and I ran a portion of the blood samples so Martin could see how we were reading —how it was done—we ran just some of the worst re-actors. * * * I gave Martin a copy of the original report."

Yet, two months after this examination, at which he, Martin, was personally present, which showed that over half his herd was contaminated, he sloughs this dying dairy business onto Sheely for the purchase price of $28,294.00; $9800.00 cash, the balance on monthly payments of $308.22, which Sheely continued to pay up to and for the month of December, besides paying the rental for the lease and grazing permit; and not a word about this examination, not a word about this blood test, even according to his own testimony, was told by Martin to Sheely.

We cite again, *Groves v. Jones,* a contagious abortion case, in which the facts were remarkably similar to the facts here, and in which the Court said:

> "The plaintiff was the innocent victim of defendant's fraud. Taking the most extreme view of the testimony against him, it shows only a suspicion on his part while the undisputed evidence shows that the defendant knew they were infected. Clearly they were not in pari-delicto or particeps criminis."

THE CONTRACT WAS ENTIRE.

Appellant cites *Hermanos v. Matos,* 81 Fed. (2d) 930, arising in Puerto Rico. That case is in point in one respect only, in that it holds that on a sale of a herd of cattle, some of which were diseased, the sale was void or voidable, only as to those cattle which were diseased, but valid as to the remainder. But as constantly urged by appellants, the appellees' purchase was of a dairy business, a going concern. (Appellants' Brief, pages 33-34, and R. 10.) True, the amended complaint alleges (R. 47, Par. V):

> "that the chief item contained in the inventory of property attached to the conditional sales agreement, 'Exhibit A', was fifty-six head of cows; that said cows were figured by the parties at three hundred dollars ($300.00) per head, which accounted for $16,800.00 of the total purchase price of $28,294.00 * * *".

Appellants' answer (R. 31) admits this allegation except "that defendants deny that there was any

segregation of value for the cows or any other item embodied in said conditional sales contract, Exhibit A".

Appellees did not by the allegation intend to allege that "there was any segregation of the value for the cows", and does not now so allege.

Appellees alleged that "the chief item contained in the inventory was 56 head of cows; that said cows were figured by the parties at ($300.00 per head.") The plaintiff, Sheely, sustained this allegation by his testimony (R. 116) and was not contradicted by any testimony of the defense.

So that, it stands uncontradicted that the cows were the chief item in the inventory of property sold by defendants to plaintiff, and accounted for $16,800.00 of the total purchase price of $28,294.00.

Furthermore, it is alleged in the complaint (R. 46, Par. III) and admitted by the answer (R. 31, Pars. I, II) that the "Conditional Sales Agreement", "Lease", and "Grazing Permit", were each an integral part of the whole transaction, neither being acceptable to the plaintiffs without the others.

Appellants agree with the statement made in appellants' brief (page 34) as follows:

> "They were actually purchasing a going business which had been in existence for years, a large number of items of personal property in addition to the cattle, together with a lease on an extensive tract of land, and there is not even an intimation that any of these other items were not lawful items of commerce."

It being conceded by the pleadings that the contract was entire, and that all three contracts constituted one transaction; and the undisputed evidence showing that at the time of the sale, a majority of the cows were infected with Bang's Disease, and that the value of the cows accounted for the greater part of the sale price, a simple question is presented to the Court for solution, to-wit:

> "Were the promises and considerations severable, so that the purchases must retain that portion of the consideration which consisted of legitimate and lawful items of commerce?"

Appellants contend that they must, and in support of their contentions rely solely on the Puerto Rico case, *Hermanos v. Matos,* 81 Fed. (2d) page 930, which, as stated in appellants' brief (page 34) involved the purchase of 122 head of dairy cattle for the sum of $18,000.00. There were no other items in the sale, and no companion contracts. Some of the cattle turned out to be tubercular, and the Court seems to have held that the cattle were sold individually, that it was a distributive sale, and that the defendant had a clear right to insist that the contract was good for the cattle that were sound.

But here we have a situation where, as so earnestly contended by appellants, the sale was of:

> "The whole of that certain dairy and milk distribution business * * * including the livestock, furniture and fixtures, farming implements and tools and motive equipment * * * and also good will;"

and where the purchase price was $28,294.00, of which $16,800.00 was accounted for by the item of 56 cows; that at the time of the sale, according to Territorial Veterinarian Graves, 29 of the cattle had Bang's Disease; according to the same witness, on January 18, 1942, all were infected except 8.

Entire and severable contracts are well defined in the note to Stearns Salt & Laneter Company, 2 *A.L.R.* p. 245, as follows:

> "The construction of contracts of this character does not depend solely or necessarily upon the nature of the articles which are the subject-matter thereof, or upon the price affixed to each article, but rather upon the nature of the contract itself. The contract is entire *if it is one bargain,* and it matters not whether there is one article, or many, each having an apportioned price."
>
> "On the other hand, a severable contract is one in its nature and purpose susceptible of division and apportionment, having two or more parts in respect to the matters and things contemplated and embraced by it, not necessarily dependent upon each other, the consideration not being single or entire as to all of its several provisions, as a whole."

And further, page 647, as an example of an entire contract, the note states:

> "or when the subject is of such a nature that the failure to obtain a part of the articles would materially affect the object or purpose of the contract, and thus having influenced the sale, had such a failure been anticipated."—citing
>
> *Pacific Timber Co. v. Iowa Windmill & Pump Co.,* 112 N.W. 771.

Further argument seems unnecessary to show that the conditional sales agreement entered into by the parties falls squarely within the foregoing definition of an entire contract. That being the case, the general rule as to the legality becomes applicable.

> "If any part of a single consideration for one or more promises is illegal, or if there are several considerations for one promise, some of which are legal and others illegal, the promise is wholly void."
>
> 13 *C. J.*, Sec. 471.

And

> "When an entire contract is illegal in part, a recovery cannot be had thereon by a renunciation of the illegal part,"
>
> "If any part of an indivisible promise or any part of an indivisible consideration is illegal, the whole is void."
>
> *East Stroudberg Nat. Bank v. Seiple,* 13 Pa. Dist. 575, 29 Pa. Co. 245.
>
> "If any part, however small, of the entire consideration of a contract is illegal, the whole is void."
>
> *Kimbrough v. Lane,* 11 Bush (Ky.) 556;
>
> *Wegner v. Biering,* 65 Tex. 506.

Here we have a situation where the larger part of the chief item of a sale consisted of diseased cows, the sale of which was illegal by statute. And it must be remembered that the contract was a conditional sale, that one of the conditions was

> "that the herd shall be maintained in not less than the present number, during the life of this contract",

a condition impossible of fulfilment, as it would require the commingling of healthy with diseased cows, or the purchase of an entire herd, preceded by a careful disinfection of the ranch premises, and the land covered by the lease and grazing permit.

RESCISSION.

It is contended by appellants that the complaint does not state a cause of action, and that there was a failure of proof, because there was neither allegation nor evidence that the appellees offered to return the consideration, the property purchased, and appellants assume, without citing authorities, that such offer of restitution was necessary, even where the contract was illegal, fraudulent and void. We find, however, that the rule as stated in 13 *C. J.*, Sec. 454, is otherwise,

> "While there are cases to the effect that, as long as a party retains the benefit of an agreement he will not be allowed to avail himself of its illegality, they are contra to the weight of authority and are opposed to the general rule already stated, it being ordinarily held that, where the contract is void because of illegality, its repudiation by one party does not give the other a right to have restored to him what he parted with under it."

But it seems unnecessary to consider this assignment. The complaint states a cause of action in damages, regardless of the prayer. No evidence was offered of consequential damage, the testimony being limited to the amounts paid by Sheely. The Court seems to have treated the case as being tried on appellants' affirmative defense, which was a suit for the entire balance alleged to be due under the contract of purchase, and defendants' reply which set up a counterclaim for return of money paid, and prayed for judgment "on plaintiffs' counterclaim for the sum of $18,164.10." (R. 59.)

The situation was exactly as it would have been had the appellants been plaintiffs, elected to terminate the contract and sued for the whole balance of the purchase price. By that said affirmative defense, appellants waive any question of an offer of restitution.

1. They pray for judgment for $16,952.90, on the sales contract;

2. For $2000.00 on the lease, and for possession of the leased premises;

3. For possession of the premises covered by the grazing permit.

They stipulated that their cause of action was of an equitable nature, but would not stipulate that the plaintiffs' cause of action was of an equitable nature. (R. 140.)

They agreed to the trial by the Court without a jury. (Appellants' Brief, page 8; Findings of Fact, R. 64.)

Appellants' conception of equity is that appellees, having paid them the sum of $14,867.95 on the several contracts involved, should now pay them another, $18,952.90, with certain interest, surrender all the premises and personal property involved to appellants, except the remnants of a diseased herd which would still be on appellants' premises, and unsalable by law except for beef.

ERRORS IN ADMISSION OF EVIDENCE.

Appellants assign as error the refusal of the Court to permit evidence of the amounts received by appellees from the sale of milk and from the sale of calves. The conditional sales agreement provided (R. 13, Par. VII),

> "that the buyers may dispose of the increase from the dairy herd in such manner as they see fit."

The Court very plainly indicated that the case was tried on appellants' affirmative cause of action for the balance of the purchase price, and appellees' counterclaim for recovery of money paid. The plaintiffs made no claim for consequential damages, which would have rendered necessary an involved accounting, in order to determine loss of profit; what they would have made had the herd been free from disease; their loss by a decrease of milk production on account of such disease; their loss on account of being forbidden by the Territorial Veterinarian, to transport the herd to cheaper pasturage, which was their privilege under paragraph Fourth of the Conditional

Sales Contract, and other elements of damage too numerous to mention.

The plaintiffs having restricted their evidence to the actual money paid, and offering no evidence of consequential damage, the Court very properly refused on Sheely's cross-examination to go into an accounting.

Possibly as stated in appellants' brief, the plaintiff, Sheely, may have made a profit in spite of "war conditions", as stated in appellants' brief (pages 40-41). Yes, possibly Sheely, despite shortage of labor, and handicapped by his Palmer ranch being rendered unavailable by law for feed and grazing, with cows dying and drying up, by his own labor and that of his wife and sons, by routing them all out in the dark hours of the Alaska morning, with the thermometer registering an average 30 degrees below zero, was able to get the cows milked, fed and watered, the barn cleaned out, the milk delivered during the few short hours of daylight, and the evening chores and milking accomplished, and was able to make wages. At any rate he tried to. At any rate, he made his payments of $308.22 per month on the contract, $200.00 per month on the lease, from July up to and including December. He struggled along under these adverse conditions, fulfilling the conditions of his contracts to the end of the year, then gave up. His complaint was verified December 27, 1941. It was not filed until May 13, 1942, possibly because the appellant, Martin, was not in the jurisdiction, but sojourning in the south (which was the fact), enjoying the profits

of a fraudulent transaction. At any rate Sheely, justifiably, made no payments after December, 1941. And Martin, according to the evidence, made no demand for further payments. Never at any time was any demand made by Martin until the filing of his answer on November 2, 1942; not until ten months have elapsed after the alleged default of Sheely, does Martin make any demand for payment, and then only when forced into Court by Sheely.

CONCLUSION.

On page 39 of appellants' brief is the following statement:

> "It is the contention of appellants that far from doing equity, the decision in this case, if it were permitted to stand, would result in about as inequitable a transaction as it is possible to imagine."

This in the face of the trial Court's findings of fact and conclusions of law, based on overwhelming evidence, to the effect that the contract was entire, illegal, against public policy and prohibited by statute; that the parties were not *in pari delicto.*

The decision awards Sheely as little as he could possibly recover under any theory of the case. As stated in appellants' brief, he was an experienced dairy man. He embarked upon an enterprise involving a large initial investment, $9800.00, and very substantial payments, contracting to pay not only a balance of $18,494.00 and interest under the condi-

tional sales agreement, but also $2400.00 per year for ten years on the lease, and $110.00 per year for ten years for the grazing permit; also $2000.00 for hay and $1700.00 for a truck; in all, a consideration of $57,094.00 and interest.

An enterprise involving this very substantial investment, and which contemplated the further investment of ten years' time of the plaintiffs' lives and labor, the investment of the plaintiff Sheely's years of experience and consequent ability and knowledge, and their application to the conduct of the enterprise. With all this investment, the plaintiffs had a right to hope, at least, for a substantial return, to retire at the end of ten years with at least a competence.

It is impossible to estimate, much less prove, the actual damage, immediate and prospective, plaintiffs have suffered by reason of defendants' wrong.

We have asked nothing for diminished profits to the date of suit, nothing for probable future losses, nor shattered hopes and prospects; for not a dollar in excess of what was actually paid. The Court has deducted from this amount every credit which could possibly be allowed to appellants.

The appellants complain that plaintiffs were allowed to amend their complaint by adding to the title the words, "Co-partners" and other allegations to conform to the proposed change. These amendments did not change the cause of action, could not possibly have in any way taken defendants by surprise, to their prejudice, they asked for no time to meet a new issue.

They complain that the complaint was amended in other particulars than those above mentioned, yet can only cite the addition of "$15,000" to the word "damages". They infer that they were hurried into the trial before the amended complaint was filed, yet did not ask for any postponement, but asked that their answer "go to the amended complaint". The trial proceeded without any objection whatever.

Appellants also complain that the Court dismissed the jury, and assigned such action as error, yet consented to such action. (Appellants' Brief, page 8; Findings of Fact, R. 64.)

We submit that judgment should not be disturbed.

Dated, Anchorage, Alaska,
August 2, 1944.

WARREN N. CUDDY,
GEORGE B. GRIGSBY,
Attorneys for Appellees.

No. 10666

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

FLORENCE DAVIS SMITH and HARVEY W SMITH,

Appellants,

vs.

THE FEDERAL LAND BANK OF BERKELEY and FEDERAL FARM MORTGAGE CORPORATION,

Appellees

OPENING BRIEF OF APPELLANTS.

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No. 10666.

IN THE

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FLORENCE DAVIS SMITH and HARVEY W. SMITH,

Appellants,

vs.

THE FEDERAL LAND BANK OF BERKELEY and FEDERAL FARM MORTGAGE CORPORATION,

Appellees.

OPENING BRIEF OF APPELLANTS.

Jurisdiction.

The Order of the District Court for the Southern District of California, Northern Division, setting aside and vacating the Findings of Fact and Conclusions of Law and Order of Hon. Leonard M. Ginsburg, Conciliation Commissioner, of December 17, 1942, and ordering that the citrus grove of the debtors be stricken from the schedules and that Appellees be permitted to exercise the power of sale under their deeds of trust was made and entered on September 17, 1943 [68-74].

Appellants' Motion for new trial, Petition for Rehearing and Motion to Vacate Judgment, Order and Findings

of September 17, 1943, was filed on October 16, 1943 [74-78] and on the same day an Order was entered by the District Judge stating that said Motion and Petition had been seasonably presented, and granting permission to file and setting the matter for hearing on October 25, 1943 [78].

On October 25, 1943, an Order was made denying said Motion for new trial, Petition for Rehearing and Motion to Vacate Judgment [102-103].

Appellants' Notice of Appeal to this Court was filed on October 27, 1943 [84-85] and served upon Appellees by mail on October 28, 1943 [85].

Orders extending time to file the record and docket the Appeal were seasonably entered on November 24, 1943 [105] and December 18, 1943 [106] extending such time to January 20, 1944. The record was duly filed on January 20, 1944 [169].

The District Court had original jurisdiction of this cause on Appellee's Petition for Review of the Order of the Conciliation Commissioner entered December 17, 1942. Section 39c of the Bankruptcy Act (Title 11, Sec. 67, U. S. Code, Ann.)

The jurisdiction of this Court is invoked under Section 24 of the National Bankruptcy Act (Title 11, Sec. 47, U. S. Code, Anno.)

Assignments of Error.

1. The District Court erred in holding that the letter of attorney, Frederick E. Stone dated March 21, 1941 and the Possession Agreement signed by Appellant, Florence Davis Smith on May 1, 1941, constituted a waiver of Appellants' rights to amend their Petition under subsection (s) of Section 75 of the Bankruptcy Act [71-73].

2. The District Court erred in refusing to grant the Motion for a New Trial, Petition for Rehearing and Motion to Vacate the Judgment in order to permit the introduction of two additional letters from Mr. Stone and a reply thereto relating to the question of the alleged waiver.

3. The Court erred in finding that there was a binding agreement to waive the benefits of subsection (s), since there was no consideration for said alleged agreement.

4. The Court erred in holding that Attorneys Frederick E. Stone and LeRoy McCormick had power by admissions to waive Appellants' rights to be adjudicated under subsection (s).

5. The District Court erred in holding that the rights of Appellants as farmer-debtors to file an Amended Petition under subsection (s) of Section 75 of the Bankruptcy Act could be waived.

6. The Court erred in holding that the term of Appellants' extension proposal expired on November 2, 1940.

Statement of the Case.

Two principal questions are presented on this Appeal:

1. Did Appellants by their conduct, waive their right to petition the Court to be adjudicated bankrupts under subsection (s) of the Bankruptcy Act?

2. As a matter of public policy, could the Appellants, as farmer-debtors, waive that right?

Appellants are farmers operating a navel orange and grapefruit grove near Porterville in Tulare County [4]. Appellees hold notes against said property secured by two trust deeds [5].

Appellants filed a Petition under Section 75(a-r) of the Bankruptcy Act in September, 1937 [2]. An Extension Proposal, dated November 2, 1937, was submitted by Appellants [3-17], accepted by the required majority of creditors [2], and approved by the then Conciliation Commissioner on December 14, 1937 [19], and thereafter approved by the Court [2-3].

On February 18, 1941, Appellees filed a Petition asking for an Order terminating the proceedings or authorizing them to proceed to sell under their deeds of trust [92-99]. On March 12, 1941, a hearing was had on this petition [46]. On March 21, 1941, Attorney Frederick E. Stone wrote a letter to Mr. Hoffmann of counsel for Appellees [166] and Mr. Hoffmann replied on March 26, 1941 [34].

The District Judge afterward held that these two documents constituted a waiver by Appellants of all right to be adjudicated under subsection (s) [65]. Three further letters between these two attorneys dated in March and early April, 1941, are in the present appeal record as exhibits to an affidavit in support of the Petition for Rehearing [81-83]. The contents of all five letters will be discussed hereafter.

On May 1, 1941, Mr. Hoffmann and Mr. Andrews, representing the Appellees, called on Mrs. Smith of Appellants and obtained her signature on a possession agreement [139-141] which the District Judge afterward held was further evidence of waiver [65] in spite of Mrs. Smith's explanation of these events [144-145, 141-142, 148].

On February 9, 1942, Conciliation Commissioner Ginsburg made certain Findings of Fact and Conclusions of Law regarding the Petition filed February 18, 1941, and ordered that Appellees with the consent of the Court might proceed to exercise their power of sale [39-43].

On June 11, 1942, Appellants' Amended Petition asking that they be adjudicated bankrupts under subsection (s) of Section 75, was filed in the District Court [20-21] with the certificate of the Conciliation Commission recommending such adjudication [22-23]. On the same day, Appellants were duly adjudicated bankrupts under subsection (s) by an Order entered by Hon. Paul J. McCormick, United States District Judge [23-24].

On July 21, 1942, Appellees filed a Petition before Commissioner Ginsburg, praying that the adjudication of Appellants under subsection (s) be set aside and vacated and these proceedings be dismissed or that Appellants' grove be stricken from the schedules [24-33]. A hearing was had before the Commissioner on September 3, 1942, and certain testimony taken of Appellant Florence Davis Smith and of Percy A. Smith of counsel for Appellees and certain offers of proof made [118-168]. On December 17, 1942, this Petition was denied by the Commissioner, who held Appellants within their rights in filing under (s). A Petition for Review was filed by Appellees [49-55], and in due course the Commissioner filed a Certificate for Review with certain exhibits attached [56-60].

In the meantime on November 2, 1942, the Commissioner entered an order directing that possession remain in Appellants, fixing the rental at $500.00 a year and staying proceedings for three years [99]. This order has never been appealed from.

Thereafter the cause came on for review before Hon. C. E. Beaumont, Judge of the District Court. In a Memorandum Opinion and Order dated and filed July 9, 1942, Judge Beaumont held that Appellants had waived their right to be adjudicated under subsection (s) [64-68] and that such waiver was shown generally by the record and particularly by the letter of Frederick E. Stone, then attorney for the Appellants, dated March 21,

1941 [166-167] and the reply of M. G. Hoffmann, attorney for Appellees, dated March 26, 1941 [34-36], and the execution of a possession agreement by Appellant, Florence D. Smith [36-38]. On September 17, 1943, Judge Beaumont entered Findings of Fact, Conclusions of Law and an Order setting aside and vacating Findings of Fact, Conclusions of Law and Order of Commissioner Ginsburg, dated December 17, 1942, and striking from the debtors' schedules, Appellants' grove.

Appellants' Motion for new trial, Petition for rehearing and Motion to vacate the Order of September 17, 1943, was filed herein October 16, 1943 [74-78] and supported by the affidavit of Allan J. Carter, present attorney for Appellants, attaching as exhibits copies of two additional letters from Attorney Frederick E. Stone to Mr. Hoffmann dated March 27, 1941 and April 3, 1941 and of Mr. Hoffmann's reply dated April 9, 1941 [79-83], which Appellants claim establish that no waiver occurred.

The District Court, on October 16, 1943, entered an Order that this Petition had been seasonably presented and set it for hearing on October 25, 1943 [78]. On the latter date an Order was made denying said Motion for new trial, Petition for rehearing and Motion to vacate [102-103]. This Appeal followed [84-85].

ARGUMENT.

I.

Appellants Did Not Waive Their Right to Be Adjudicated Bankrupts Under Subsection (s) of Section 75 of the Bankruptcy Act.

The District Judge in his Memorandum Opinion [65] and in his Findings [71-73] and Conclusions of Law [73] reversed the Conciliation Commissioner and held that Appellants had waived all right to be adjudicated under subsection (s) in so far as the grove was concerned.

This ruling in effect amounted to the setting aside of the adjudication under (s) and a dismissal of the proceedings, since the grove was the only real estate held by Appellants [4-5].

The District Court held that the letter dated March 21, 1941, from Mr. Frederick E. Stone, then attorney for Appellants, to Mr. Hoffmann, one of Appellees' attorneys [166], and Mr. Hoffmann's reply of March 26, 1941 [34], and the possession agreement signed by Mrs. Smith on May 1, 1941 [36], constituted a waiver [65, 71-73].

We respectfully submit that a study of these three documents together with an analysis of Mrs. Smith's testimony and offers of proof [123-165] establish that there was in fact no waiver made.

It is true that Mr. Stone in his letter of March 21, 1941, did say that he had discussed the matter of going under (s) with Appellants and that they had concluded to abandon the property and let the matter go by default if the Randolph Marketing Company could be protected

as to the grapefruit then on the trees. However, Mr. Stone wound up that letter with a statement that he would appreciate an immediate reply since he was "holding the matter in abeyance" pending an answer [167]. Across the bottom of this original letter was a notation by Mr. Andrews of the Federal Land Bank [139] reading in part as follows:

> "O. K. to *consent to Randolph harvesting and marketing grapefruit* for returns *up to their outlays. If Smiths will request dismissal of proceedings so we can proceed to F. C.*—also Smiths give possession to Bank so as to care for property pending F C sale" [167]. (Emphasis ours.)

Mr. Hoffmann's reply of March 26, 1941, did not accept the alleged waiver *proposal* made in Mr. Stone's letter but on the contrary attached conditions to any acceptance which were never at any time complied with.

Mr. Hoffmann's letter read in part:

> *"We hereby agree that, if the debtors will withdraw their opposition to our petition and consent to the Conciliation Commissioner's order which was prayed for therein,* and *if* the Conciliation Commissioner will make the order either recommending the dismissal of the proceedings, *and such recommendation is followed by a dismissal order signed by a judge, or if the Conciliation Commissioner will make an order authorizing us to proceed with trustee's sale under one or both of our deeds of trust, and if the debtors will, after entry of the necessary order, execute and return the enclosed possession agreement,* the Randolph Marketing Company shall have the right to enter upon the property, pick the grapefruit and retain from the proceeds thereof, in so far as such pro-

ceeds shall be sufficient, the sum necessary to reimburse said marketing company for outlays made under authority of the Conciliation Commissioner, for the upkeep and care of the property.

"* * * *we see no reason for authorizing the Randolph Marketing Company to take more of the proceeds than will be necessary to reimburse it for such advances.*

"In order to expedite the matter we are also enclosing an order which may be signed by the Conciliation Commissioner. We prefer to have this order signed at once and a conformed copy returned to us with the executed possession agreement. Thereafter we believe it would be advisable for you to present to the Conciliation Commissioner a petition for dismissal of the proceedings, signed by the debtors. The Commissioner should endorse his recommendation on such petition and forward it to the judge. Since the proceedings are merely under Section 75(a-r), we believe that they may be thus dismissed summarily" [35-36]. (Emphasis ours.)

The conditions that debtors must withdraw their opposition to Appellees' petition and must consent to the Conciliation Commissioner's order prayed for in said petition were neither of them ever met. The Conciliation Commissioner never made an order of dismissal. While nearly a year later he made an order authorizing the Appellees to proceed with the Trustee's sale, that order recited that Appellees might "with the consent of this Court proceed to have the power of sale * * * exercised." If the

Commissioner's language in the phrase just quoted meant that he was giving the consent of the Court by that Order, such was beyond his power under subsection (o) of Section 75 of the Act since only a District Judge had that power. If he meant that an Order was to be obtained from a Judge of the District Court, no such Order was ever obtained.

The actual suggestion in Mr. Stone's letter of March 21st was that Mr. Avery, of the Randolph Marketing Company was to take all of the grapefruit on the trees. Mr. Hoffmann's reply was limited in its tentative consent, subject to conditions which were never met, to whatever sum was necessary to reimburse Randolph Marketing Company for its advances.

Mrs. Smith testified that the possession agreement enclosed with Mr. Hoffmann's letter of March 26th contained a phrase admitting that Appellants had had a fair trial under subsection (a-r) and were unable to show any results and were willing to voluntarily ask the Commissioner to dismiss the case [142]. Appellants refused to sign this and later in May, 1941, accompanied by Mr. Hoffmann, Mr. Andrews brought another agreement which omitted all that objectionable part [141-142].

Mr. Shirley, then attorney for Appellants, offered to prove by Mrs. Smith that Mr. Andrews misstated the effect of this modified possession agreement which she did sign on or about the 1st of May, 1941, telling her "that the Bank didn't have any intention of doing anything ex-

cept working the grove, and * * * that the agreement just covered the right to work the grove and that was the extent of it" [144-145, 141-142, 148]. Mrs. Smith further testified that when she did sign this possession agreement, no consideration was given [149].

Mr. Shirley further offered to prove by Mrs. Smith that the Bank induced her by "hallucinations on its part, and conversations, to wait; and that she was depending upon them to take some action which they never took to work out the situation in a manner that would not require her to go under (s)" [153, 159].

Mrs. Smith further testified that she never gave any indication to the Bank or any of its officers that she was willing to give up or waive her rights under subsection (s) and that she never authorized anybody else to do that in her behalf [155-157].

Clearly these facts even as interpreted by the District Judge, do not amount to a waiver as a matter of law. It has been held by the Federal Courts that the essence of waiver is estoppel and that the party claiming the waiver must have been misled and must have changed its position.

Amsinck & Co. v. Springfield Grocer Co., 7 Fed. (2d) 855, 860.

In the present case, Appellees were not misled and never changed their position. The three documents relied on as constituting the waiver were dated in March and May, 1941 and yet up to June 11, 1942, when Appellants were adjudicated bankrupts under subsection (s)

there is no evidence of any change of position by Appellees. Surely one cannot stand by without taking any action in reliance on the alleged waiver and even take other inconsistent steps and then afterward claim there was a waiver.

From the above review of the evidence actually before Commissioner Ginsburg, we submit that he was justified in holding that Appellants were entitled to be adjudicated under subsection (s). While in his Order of December 17, 1942, the Commissioner did not refer to waiver or estoppel, those questions had been raised by paragraph 12 of the Petition to Dismiss, filed before him [31].

It has frequently been held that a District Judge should not reverse a Conciliation Commissioner where the Judge himself hears no new evidence unless the facts are capable of only one interpretation or unless the Commissioner acted on an entirely erroneous view of the law. (*Dunsdon v. Federal Land Bank,* 137 Fed. (2d) 84 and 53 Am. B. 488.)

Here Judge Beaumont had to hold that the Commissioner was wrong, both as to law and facts in order to reach a contrary conclusion. We respectfully submit that the District Judge has attempted to read into Mr. Stone's letter of March 21, 1941 [166] an unqualified waiver which was not there and to entirely disregard the conditions set up in Mr. Hoffmann's reply [34] which were never complied with and also to disregard the uncontradicted testimony of Mrs. Smith regarding the circumstances occurring when she signed the possession agreement [144-145, 141-192, 148], all of which additional evidence establishes that no waiver was in fact made.

II.

The District Court Should Have Granted the Petition for Rehearing in Order to Permit the Presentation of Further Oral and Documentary Evidence to Show There Was No Waiver.

We have pointed out that the evidence received by the Commissioner was sufficient to establish that Appellants did not waive their right to be adjudicated under (s) and that the District Court erred in holding otherwise. Even if his decision had been justified on the evidence before him, it would still have been his duty on the showing made on the Petition for Rehearing by the affidavit of Allan J. Carter and the three letters set forth there as exhibits, to have opened the case up for further evidence.

There have been at least three different attorneys representing appellants prior to present counsel, two of them having been called into the armed services [63]. The record of the hearing before Commissioner Ginsburg on September 3, 1942, shows that Mr. Marlin H. Shirley who had then succeeded Mr. Stone, assumed that all the letters making up the correspondence between Mr. Hoffman and Mr. Stone were in the record [122, 133, 163].

At the very end of that hearing, this colloquy took place between counsel:

> "Mr. Shirley: Are we agreed that all these letters on the part of the bank are introduced into evidence, Mr. Smith?
>
> Mr. Smith: Make an offer. He previously ruled that the letters were all part of the record in the case.

Mr. Shirley: Well, that is all I wanted to know.

Mr. Smith: The entire record is in evidence" [163].

Certainly Mr. Shirley was justified by Mr. Percy Smith's statement in assuming that all letters written by the Land Bank as to this point were in the record. The Commissioner said he didn't choose to take time for Mr. Shirley "to read all the letters in the file" but that they could all be read by the District Judge or whoever had to decide the case [163].

However, when the case came to be heard by Judge Beaumont, Mr. LeRoy McCormick had succeeded Mr. Shirley as counsel for Appellants [64] and only the two letters heretofore commented on were before the Court. When the undersigned followed Mr. McCormick as counsel for Appellants he obtained from Appellants carbons of two further letters which Mr. Stone sent to Mr. Hoffmann and the original of Mr. Hoffmann's reply of April 9, 1941. Copies of these were then set up as exhibits in support of the petition for rehearing [81-83].

When considered with the earlier letters, these three documents show conclusively that our interpretation of those earlier letters above set forth, was correct and that there had been no waiver.

Mr. Stone received Mr. Hoffmann's letter of March 26th on the following day, March 27, 1941, and answered it at once, saying:

> "*I have forwarded your letter* and one copy of each document *to the Smiths for their consideration. Just*

as soon as they advise me whether or not they are willing to enter into the agreement as suggested by you, I will in turn immediately notify your office.' [81.] (Emphasis ours.)

On April 3, 1941, Mr. Stone wrote again to Mr. Hoffmann that the Smiths had gone over the matter, but before proceeding, they wanted to find out whether the Land Bank would consider a scale down arrangement "whereby the debtor might pay off the indebtedness and keep the property" [82].

On April 9, 1941, Mr. Hoffman replied that they could not agree to a voluntary scale down. He concluded his letter with the statement:

> "We would like very much to have the matter handled as suggested in our last letter, if Mr. and Mrs. Smith have not changed their minds" [83].

This letter did two very important things. It again insisted on the conditions set out in the letter of March 21 which we have seen never were met by Appellants. Also, it showed that the Land Bank, realizing that the Smiths might have changed their minds, was not relying on any waiver. The uncontradicted fact that three weeks later on May 1, 1941, Mr. Hoffmann and Mr. Andrews were presenting a modified form of possession agreement to Mrs. Smith [139-141] shows that the Land Bank was pursuing a different course. So far as the record discloses, nothing further was ever said about Appellants filing a consent dismissal and none was ever filed.

Clearly there never was any waiver.

III.

There Was No Valid Consideration for Any Waiver Agreement.

The District Judge in his Memorandum Opinion and in his Findings has treated the exchange of the two letters of March 21 and March 26, 1941 as constituting a binding agreement between the parties. Even if it had been an agreement, it would not have been an enforceable contract because there was no valid consideration moving to Appellants. This point was made by Mr. Shirley at the hearing on September 3, 1942 [139]. Mrs. Smith testified there was no consideration [149] and Mr. Shirley stated that the record showed the Randolph Marketing Company already had the right to market the fruit [149].

In a somewhat similar situation, the Circuit Court of Appeals for the Eighth Circuit held that there was no consideration for the agreement admittedly made: *Buss v. Prudential Insurance Co.*, 126 Fed. (2d) 960. In that case a farmer filed under Section 75 without joining his wife who owned a half interest as a tenant in common. After failing to reach an agreement with his creditors, he filed under subsection (s). Thereafter the creditor asked leave to proceed with foreclosure of its mortgage. The attorney for the farmer then signed and filed a written agreement consenting to foreclosure and the appointment of a receiver who was to lease the farm to the farmer for two years on crop share rental which would go to the farmer if the property was redeemed, other-

wise to the mortgagee. That proceeding under (s) was afterward dismissed and no appeal taken.

Later the farmer and his wife filed a new joint proceeding under Section 75 which was dismissed by the District Court on recommendation of the Commissioner on the ground that the former proceeding was *res adjudicata*. That decision was reversed by the Court of Appeals. Concerning the signed agreement, the Court said, page 965:

> "The record of the former proceeding under the statute by Walter Clifford Buss is set out in full, and is admitted. Buss admits that an agreement was made in that proceeding but says that he never saw it. The agreement in the record appears to have been signed by counsel. There is no evidence to the effect that either appellant ever received any consideration for the agreement. There is no showing that the agreement was ever performed by either party to it."

So in our case, there was no consideration and therefore on this separate ground the holding of the District Court should be reversed.

IV.

Neither Mr. Stone Nor Mr. McCormick Had Any Power to Waive Appellants' Rights to Be Adjudicated Under (s) Nor Did They Intend to Waive Such Rights.

Generally an attorney has no right to compromise a Cause of Action without express authority so to do.

Barber-Coleman Co. v. Magnano Corporation, 299 Fed. 401.

Note 66 A. L. R. 108 and cases there cited.

This rule applies with even greater force to a release or waiver of a right and it has been so held by this Court:

Bruun v. Hanson, 103 Fed. (2d) 685, at 701.

In the absence of a specific authority the client must acquiesce after full knowledge of all the facts, before being bound. No such acquiescence occurred here as to Mr. Stone's letter of March 21, 1941. On the contrary as we have seen the later correspondence shows that he consulted the clients and they declined to do the things Appellees insisted must be done before they would agree to any program.

The position is very much weaker as to the alleged waiver by Mr. McCormick in his statement of facts [63]. He merely said that Appellees' statement of facts "appears to be substantially borne out by the admission of debtors." This was merely a loosely phrased legal conclusion which is never binding on a client as an admission.

5 *Amer. Jur.* par. 94, page 316.

V.

The Right of a Farmer-Debtor to Be Adjudicated a Bankrupt Under Subsection (s) Cannot Be Waived.

The fundamental benefits of Section 75 of the Act were granted to the farmers as a class.

Paradise Land & Livestock Co. v. Federal Land Bank 108 Fed. (2d) 832 at 834;

In re Loose, 52 Fed. Supp. 20 at 24.

It has been repeatedly held that under Section 75 of the Act the farmer can not waive any of his substantive rights nor any of the essential elements of the procedure set up by the statute.

Borchard v. California Bank, 310 U. S. 311, 84 L. Ed. 1222, 60 S. Ct. 957;

Wright v. Logan, 315 U. S. 139, 84 L. Ed. 443;

Paradise Land and Livestock Company v. Federal Land Bank, 118 Fed. (2d) 215;

Corey v. Blake, 136 Fed. (2d) 162.

It has been held that an agreement to waive the benefit of the general bankruptcy act is void. This was decided in the case of *In re Weitzen*, 3 Fed. Supp. 698, 23 A. Bn. 653. The District Judge there said, page 698:

> *"The agreement to waive the benefit of bankruptcy is unenforceable. To sustain a contractual obligation of this character would frustrate the object of the Bankruptcy Act, particularly of section 17* (11 U. S. C. A., sec. 35). This was held by the Supreme Judicial Court of Massachusetts, *Federal Nat. Bank v. Koppel,* 253 Mass. 157, 148 N. E. 379, 380, 40 A.

L. R. 1443, where it was said: 'It would be repugnant to the purpose of the Bankruptcy Act to permit the circumvention of its object by the simple devise of a clause in the agreement out of which the provable debt springs, stipulating that a discharge in bankruptcy will not be pleaded by the debtor. The Bankruptcy Act would in the natural course of business be nullified in the vast majority of debts arising out of contracts, if this were permissible. It would be vain to enact a bankruptcy law with all its elaborate machinery for settlement of the estates of bankrupt debtors, which could so easily be rendered of no effect. The bar of the discharge under the terms of the Bankruptcy Act is not restricted to those instances where the debtor has not waived his right to plead it. It is universal and unqualified in terms. It affects all debts within the scope of its words. *It would be contrary to the letter of section 17 of the Bankruptcy Act as we interpret it to uphold the waiver embodied in this note. So to do would be incompatible with the spirit of that section. Its aim would largely be defeated.*'" (Emphasis ours.)

A similar statement of this same rule was made by Hon. Ralph E. Jenney of our District Court in connection with a reorganization proceeding under Section 77(B) of the Bankruptcy Act. This was the case of *In re Los Angeles Lumber Products Co., Ltd.*, 24 Fed. Supp. 501, 47 A .Bn. 688, where it was urged that the language of a trust indenture precluded the debtor corporation from voluntarily taking advantage of Section 77(B) of the Act. Judge Jenney said, page 515:

"* * * *any such attempted restriction upon the debtors' rights even in a voluntary proceeding would seem to this court to be void, as contrary to public*

> *policy.* The court does not believe that the company could place itself, or that the bondholders did place themselves by this agreement which is binding upon all parties, in such a position that advantage could not be taken of this section of the Bankruptcy Act. In that connection see: *In re Weitzen,* D. C. 3 F. Supp. 698, 23 A. B. B., N. S., 653; *Federal National Bank v. Koppel,* 253 Mass. 157, 148 N. E. 379, 40 A. L. R. 1443, t A. B. R., N. S., 287." (Emphasis ours.)

This same doctrine has been applied recently in several farm-debtor cases.

In *Trego v. Wright,* 111 Fed. (2d) 990, the farmer's property was sold under foreclosure on July 21, 1934. Five days before the sale took place, the farmer asked the State Court to postpone the sale to February 1, 1935. The State Court then entered a formal Order reciting (p. 990) that:

> "By agreement of the parties * * * the sale * * * will not be confirmed until the defendant, Grover C. Trego shall have reasonable opportunity to redeem * * * but in no event shall the time for redeeming said premises extend beyond the first day of February, 1935."

The farmer did not redeem his property and the sale was confirmed February 11, 1935. In the meantime on January 26, 1935, the farmer filed a petition in the Federal Court under Section 75. His offer of composition was rejected and on November 6, 1935, he was adjudicated

a bankrupt under subsection (s). A year later he asked the Federal Court to vacate the orders made by the State Court confirming the sale of his property. The District Court dismissed the proceedings under Section 75 saying among other things that the State Court had merely carried out the terms of the farmer's agreement made in open court. The Circuit Court of Appeals in reversing the District Court, said in part, page 991:

> "Unless the agreement above quoted estops appellant from taking advantage of the provisions of Section 75, subsection s, clearly the order of the District Court must be reversed. * * * Neither did the agreement made by the appellant prior to the second enactment of subsection s, estop appellant from asserting his rights under the amendment. The agreement did not waive the right to assert such rights, and *if it had it would have been void as against public policy.*" (Emphasis ours.)

A similar result was reached by the same Circuit Court of Appeals in the later case of *Federal Land Bank v. Morrison,* 133 Fed. (2d) 613. In that case, during the (a-r) proceedings, the debtors consented to the appointment of a receiver. Afterward, the debtors were adjudicated bankrupts under subsection (s). Concerning the consent agreement to the appointment of the receiver, the Circuit Court of Appeal said, page 617:

> "This is true irrespective of the consent agreement. *The debtors and creditors could not waive nor modify the provisions of Section 75. Trego v. Wright,* 6

> Cir., 111 F. (2d) 990. A similar stipulation between secured creditor and debtor, dealing with the disposition of the proceeds of crops harvested on the debtor's premises, was held by the Supreme Court in *Borchard v. California Bank,* 310 U. S. 311, 317, 60 S. Ct. 957, 84 L. Ed. 1222, to be part of a 'procedure not contemplated by the statute'." (Emphasis ours.)

In the case of *Hepker v. Equitable Life Assurance Society,* 131 Fed. (2d) 926, the farmer, after filing under (a to r) and while attempting to work out a composition orally agreed in the presence of the Commissioner that if negotiations for compostion failed she would pay rent for the year 1941 in an amount to be fixed by the Commissioner. The negotiations failed and the farmer filed under (s) on August 5, 1941. The Commissioner thereafter ordered rent to be paid from March 1, 1941. The District Judge modified this by requiring rent from date of adjudication. The mortgagee on cross-appeal attempted to sustain the requirement to pay rent from March 1st relying on the farmers' agreement. The Circuit Court of Appeals said, page 927:

> "It is argued that the agreement may be treated as a waiver by the debtor of her right to have the rent order fixed in due course of bankruptcy proceedings under the statute, but *we think the statute and not the agreement made six months before bankruptcy must control.* The relief sought by the cross appeal is denied." (Emphasis ours.)

VI.

The Term of Appellants' Extension Proposal Did Not Expire on November 2, 1940, and the Findings of the Commissioner and of the District Court Covering That Point Should Be Set Aside.

While we believe that the several propositions discussed above require a reversal of the Order entered by the District Court on September 17, 1943, without regard to the Court's finding that Appellants' extension proposal expired on November 2, 1940, nevertheless we believe that finding was erroneous and should be corrected. The extension proposal itself did not express November 2, 1940, as a termination date [3-19]. That proposal after setting up a plan for the first year of the extension period [11], had a sub-heading [15]:

> "During second, third years and remaining portion of said extension."

The opening sentence under this heading read [15]:

> "That during the second and third years of said proposal and said extension, and during the balance of any extended period given to these debtors * * * said debtors propose * * *"

We submit that the above heading and opening phrases would each be meaningless unless they referred to some period after the end of the third year.

At the hearing in the District Court, it was claimed that since a similar finding that the extension proposal

had expired on November 2, 1940, was included in the findings of Commissioner Ginsburg's Order of February 9, 1942, and no appeal was taken from that Order, the finding had become *res judicata* against appellants.

Appellants' position is that the Commissioner's Order of February 9, 1942, was void and not voidable for the reason that under Section 75 of the Act, the District Judge was the only one who had power to permit a creditor to foreclose. This power is set up in subsection (o) of Section 75 of the Act. This subsection reads in part:

> "Except upon petition made to and granted by the Judge after hearing and report by the Conciliation Commissioner, the following proceedings shall not be instituted * * *.
>
> "(2) Proceedings for foreclosure of a mortgage on land * * *"

A leading decision construing this subsection is one by this Court in *McFarland v. Westcoast Life Insurance Co.*, 112 Fed. (2d) 567.

It is true that this subsection also contained the phrase "prior to the confirmation or other disposition of the composition or extension proposal by the Court," which this Court has held meant that the restriction against further action by a state court was not automatically stayed by adjudication under (s); *Hardt v. Kirkpatrick*, 91 Fed. (2d) 875. Nevertheless, it has been construed in the light of more recent decisions of the United States Supreme Court, to control as to matters arising in later proceedings under Section 75. (*Bastian v. Erickson*, 114 Fed. (2d) 338 at 340.) Applying this construction to the present

case, Commissioner Ginsburg had no authority whatever to issue an Order permitting Appellees to proceed to foreclose and any attempt on his part to do so was void and not merely voidable.

We have already referred to the phrase in his Order of February 9, 1942, "with the consent of this Court." If that phrase meant that he was submitting a report to the Judge for his consideration and action, it was proper procedure but since that Order never was presented to any District Judge for his approval, no Order on the subject ever became effective. If, by the phrase quoted, the Commissioner meant that he was by his own Order, giving the Court's consent, we submit that it was beyond his power to do so.

Even if the Commissioner's finding were merely voidable and not void, it would still be subject to being set aside and vacated unless rights have become vested in reliance upon it which will be disturbed by its being set aside. (*Wayne United Gas Co. v. Owens Illinois Gas Co.*, 300 U. S. 131, 136-137, 81 L. Ed. 557 at 561, 60 S. Ct. 773; *Wharton v. Farmers and Merchants Bank*, 119 Fed. (2d) 487 at 489.)

There is no evidence whatever in the present record to indicate that Appellees did anything between the time of the entry of Commissioner Ginsburg's Order of February 9, 1942, and June 11, 1942, when Appellants were adjudicated bankrupts under subsection (s). Nor is there any evidence that Appellees have done anything which has changed their position, even up to this date.

The similar finding by the Commissioner that the extension proposal expired November 2, 1940, in his Order of

December 17, 1942, sustaining Appellants' right to be adjudicated under (s) and an identical finding by Judge Beaumont in his Order of September 17, 1943, are now properly before the Court on this Appeal and therefore subject to being set aside as being contrary to the terms of the extension proposal itself as set forth above.

If we are correct in the proposition that the extension proposal did not provide for its termination on November 2, 1940, any attempt by either the Commissioner or the District Judge to alter the terms of the proposal by providing such a termination date, other than by the procedure outlined in subsection (1) of Section 75 of the Bankruptcy Act, would be void as an attempt to modify the contract rights of the debtors herein under said extension proposal agreement in violation of the Constitutions of the United States and the State of California.

Conclusion.

We respectfully submit that on all of the grounds above set forth, the orders of the District Court of September 17, 1943, and October 25, 1943, should be reversed, and Appellants be permitted to continue operating the grove under subsection (s) continuing to pay the rent provided for under the stay order of November 2, 1942.

Respectfully submitted,

ALLAN J. CARTER,

Attorney for Appellants.

No. 10666

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

FLORENCE DAVIS SMITH and HARVEY W. SMITH,
Appellants,

vs.

THE FEDERAL LAND BANK OF BERKELEY and FEDERAL FARM MORTGAGE CORPORATION,
Appellees.

BRIEF OF APPELLEES

RICHARD W. YOUNG,
M. G. HOFFMANN,
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No. 10666

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

FLORENCE DAVIS SMITH and HARVEY W. SMITH,
Appellants,

vs.

THE FEDERAL LAND BANK OF BERKELEY and FEDERAL FARM MORTGAGE CORPORATION,
Appellees.

BRIEF OF APPELLEES

CHRONOLOGICAL HISTORY OF PRESENT PROCEEDINGS

July 21, 1942 — Petition and Motion of Appellees before the Conciliation Commissioner for authorization to sell the real property covered by the deeds of trust according to state law. (R. 24-38)

September 3, 1942 — Hearing before Conciliation Commissioner on said Petition and Motion. (R. 118-168)

December 17, 1942 — Denial by Conciliation Commissioner of Appellees' Petition and Motion.

January 8, 1943 — Petition by Appellee for review of Conciliation Commissioner's denial of said petition. (R. 48-56)

May 10, 1943 — Hearing on Petition for Review before Honorable Campbell E. Beaumont, District Judge.

July 9, 1943 — Memorandum Opinion and Order of Judge Beaumont overruling Conciliation Commissioner's denial of Appellees' Petition and Motion and authorizing

Appellees to exercise the power of sale contained in the deeds of trust. (R. 64-68)

September 17, 1943 — Findings of Fact, Conclusions of Law, and Order of Judge Beaumont in accordance with his Memorandum Opinion. (R. 68-74)

October 16, 1943 — Appellants' Motion for New Trial, Petition for Rehearing of Review of Order of Conciliation Commissioner (December 17, 1942) and Motion to Vacate Judgment, Order and Findings On Review (September 17, 1943). (R. 74-78)

October 25, 1943 — Hearing before Judge Beaumont on Appellants' Motion for New Trial, etc., and the Court's denial thereof. (R. 102-103)

October 27, 1943 — Appellants' Notice of Appeal filed covering both the "order and judgment" of September 17, 1943, and of October 25, 1943.

For further brief statement of facts see pages 61-62 of Transcript of Record.

JURISDICTION

Neither the Trial Court Nor This Court Could Take Jurisdiction Over Appellants' Motion for New Trial

Rule 59, Fed. Rules of Civ. Proc., govern such motions. Even without such Rule, it would be elementary that such a motion would have been proper only if addressed to the Conciliation Commissioner following the hearing before him on September 3, 1942. A motion for new *trial* may be entertained by the *trial* court but not by a reviewing court. It is too late to file such a motion after a decision on a petition for review. This is especially true, in such cases as this, where neither the reviewing court nor the moving party requested the introduction and consideration of further evidence.

Order Denying Petition for Rehearing Is Not Appealable

Appellants also included with their motion for new trial a "Petition for Rehearing of Review of Order of Commissioner Ginsburg Dated December 17, 1942." (R. 74-78) This petition was denied by Judge Beaumont on October 25, 1943. (R. 102-103) Appellants are here attempting to appeal from the order denying the rehearing.

> "The granting of a rehearing is within the court's sound discretion, and a refusal to entertain a motion therefor, or the refusal of the motion, if entertained, is not the subject of appeal." (*Wayne United Gas Co.* v. *Owens-Ill. Glass Co.*, 300 U.S. 131, 57 S.Ct. 382)

The Question Raised in Appellants' Sixth Assignment of Error Is Res Judicata

Appellants' sixth assignment of error is as follows:

> "6. The Court erred in holding that the term of Appellants' extension proposal expired on November 2, 1940."

The Conciliation Commissioner, in his Findings of Fact and Conclusions of Law, dated February 9, 1942 (R. 39-43), expressly found that:

> "Subject to the terms of the proposal, the debtors should have an extension for three years from the second day of November, 1937; that the term of said extension proposal has expired; . . . that the debtors are in default under the terms of said extension proposal; that the extension provided therein has terminated . . ."

The Appellees were authorized to foreclose.

No appeal was taken from this action of the Conciliation Commissioner.

Appellants now contend, in order to escape the results of not appealing from such Findings of Fact, Conclusions of

Law and Order of the Conciliation Commissioner, that the order was void for the reason that "the District Judge was the only one who had the power to permit a creditor to foreclose." (Appellants' Brief, p. 26)

We submit that the question is res judicata since no timely appeal was taken. A motion to re-open and review a proceeding, such as was made by the Appellants, can not be substituted for an appeal. *Wragg* v. *Federal Land Bank of New Orleans,* 63 S.Ct. 273.

Futhermore, the order of February 9, 1942, (R. 32) amounted to a relinquishment of the bankruptcy court's jurisdiction over the property which was subject to Appellees' deeds of trust. Even assuming such order was *erroneous,* the Supreme Court has on at least two occasions expressly stated that an erroneous order may be attacked *only on appeal. Union Joint Stock Land Bank of Detroit* v. *Byerly,* 60 S.Ct. 773; *Bernards* v. *Johnson,* 62 S.Ct. 30.

In the event this Court should decide that the question of the expiration of the extension agreement is a proper subject of inquiry, Appellees call attention to the only correct interpretation of the two portions of the extension proposal quoted by Appellants on page 25 of their brief. It is true that one of the headings reads:

"During Second, Third Years, *and Remaining Portion of said Extension.*"* However, the reason for the use of the emphasized portion of the heading becomes very obvious upon reading the body of the proposal, following said heading. It is as follows:

> "That during the second and third years of said proposal agreement and said extension, and during the balance *of any extended period given to these debtors* for the payment of their secured and unsecured claims, etc."

*Throughout brief all emphasis is added to quotations.

This clearly shows that the original period of the extension was three years, but that the debtors hoped that, if they made a satisfactory showing during the three years, an "extended period" might later be given to them. In other places in the proposal reference is made to "the term of this proposal agreement *and the extension period.*" (R. 11)

There is nothing in the record which shows that any extended period was ever given to these debtors.

ISSUE BEFORE THIS COURT

The sole question before this Court on Appellants' appeal is: Did the District Judge err in making and entering his order of September 17, 1943? Said order reads:

> "Wherefore, by reason of the aforesaid findings of fact and conclusions of law, it is ordered, adjudged and decreed that the findings of fact, conclusions of law and order dated December 17, 1942, made by Leonard M. Ginsburg, Conciliation Commissioner, acting as Referee, be and the same are hereby set aside and vacated;
>
> "It is further ordered, adjudged and decreed that the property described in paragraph II of the above findings of fact be stricken from the debtors' schedules, and that The Federal Land Bank of Berkeley and the Federal Farm Mortgage Corporation, or either of them, may proceed to have the power of sale in one or both of the deeds of trust hereinabove mentioned exercised in accordance with the laws of the state of California."

There being but the one issue, Appellants' Assignments of Error Nos. 2 and 6 pertain to matters which are not properly before this Court. The remaining assignments, Nos. 1, 3, 4 and 5 are all directed to the question of whether the court erred in basing said order on a waiver of Appellants' right to amend under Subsection (s). Although Appellees believe that Appellants *did not have the legal right* to file an amended petition and be adjudicated bankrupts under Sub-

section (s), and, therefore, had nothing to waive, the question of waiver will first be considered.

ARGUMENT

I

There Was an Express Waiver by Agreement

Appellants' first Assignment of Error reads as follows:

> "1. The District Court erred in holding that the letter of attorney, Frederick E. Stone dated March 21, 1941, and the Possession Agreement signed by Appellant, Florence Davis Smith on May 1, 1941, constituted a waiver of Appellants' rights to amend their petition under subsection (s) of Section 75 of the Bankruptcy Act."

On February 18, 1941, Appellees filed a Petition and Motion with the Conciliation Commissioner, (R. 92-99) which, although no part of the phase of the proceedings now before this Court, has a bearing thereon. A hearing on said Petition and Motion was held March 12, 1941. (R. 39) Appellants were represented by Attorney Frederick E. Stone. The petition was based upon the allegation that the period of the voluntary extension under Subsec. (a-r) had expired. Appellees sought authority to have the power of sale in their deeds of trust exercised.

On March 21, 1941, Attorney Stone wrote the letter (R. 166-167) which was the basis for Judge Beaumont's conclusion that the debtors had waived their right to file an amended petition under Subsection (s). The letter stated:

> "The matter of filing a petition under Subsection (s) has been thoroughly discussed with Mr. and Mrs. Smith, the above named debtors. They have concluded that they will abandon the property and simply let the matter go by default, if the Randolph Marketing Company and their agent, Mr. Omer Avery of this city can be

> protected as to the present grapefruit crop which is now on the trees . . . If you are willing to allow Mr. Avery to take the grapefruit crop now on the trees, the Smiths are willing to let the matter go any way that is satisfactory to you."

It is evident that the *Appellants* concluded not to file an amended petition under Subsection (s) "if the Randolph Marketing Company . . . can be protected as to the present grapefruit crop."

This was the only condition imposed by Appellants. They knew that Appellees intended to sell under their deeds of trust, or one of them, and that such sale might be made before the grapefruit crop, then on the trees, could be harvested. Under California law growing crops pass to a purchaser at a trustee's sale. *Penryn Fruit Co.* v. *Sherman-Worrell Fruit Co.*, 76 Pac. 484; *Phillips* v. *Pacific Land & Title Co.*, 2 P.(2d) 566.

In the letter of March 26, 1941, the attorney for Appellees replied to the above letter, and stated:

> "We hereby agree that . . . the Randolph Marketing Company shall have the right to enter upon the property, pick the grapefruit and retain from the proceeds thereof . . . the amount necessary to reimburse said marketing company . . ." (R. 35)

The debtors withdrew their opposition and consented to the Conciliation Commissioner's order. The Court so found in its order of February 9, 1942, as follows:

> "(3) That the debtors have consented that such relief as was demanded by the secured creditors in said petition and as may be deemed proper by this Court, may be granted." (R. 41)

The Court further ordered (R. 43) as follows:

> "Wherefore, by reason of the aforesaid Findings of Fact and Conclusions of Law, it is Ordered that The Federal

> Land Bank of Berkeley and the Federal Farm Mortgage Corporation, or either of them, may, with the consent of this Court, proceed to have the power of sale in one or both of the deeds of trust hereinabove mentioned exercised in accordance with the laws of the State of California."

Appellants contend (Appellants' Brief, p. 10) that the phrase "with the consent of this Court" might be construed to mean that, although the order was made by the "Court" (See Sec. 1(9) of the Chandler Act), a *further consent* of the court was contemplated. We submit that the phrase "*with the consent of this Court*" was included for the purpose of expressly *consenting* to the trustees' sales. No further order or consent was necessary.

Appellants assume that Appellees' Petition and Motion (R. 92-99) was filed in accordance with the procedure prescribed in Subsec. (o). It was not, and, therefore, the provisions of Subesc. (o) were not applicable. Subsec. (o) is applicable only "*after the filing of the petition*" and "*prior to the confirmation* or other disposition of the composition or extension proposal by the court." The extension proposal had been confirmed long before the filing of this petition. All hearings were *required* to be held before the Conciliation Commissioners. (Rule 220, Bankruptcy Rules, U.S. Dist. Ct., So. Dist. of Calif.)

In their first Assignment of Error Appellants say the District Court "erred in holding that the letter . . . *and* the Possession Agreement . . . constituted a waiver." The District Court did not so hold. Findings of Fact, XII, states that, by reason of the offer in the letter of March 21, 1941, and its acceptance, *the debtors waived their rights.* (R. 73) In his Memorandum Opinion and Order (R. 64-65) the District Judge did state that the waiver "is shown generally by the record and particularly by the letters . . . and the *execution* of the possession agreement by Florence Davis Smith." In

other words, the fact that *after* the exchange of the letters Florence Davis Smith *executed* the Possession Agreement supported his conclusion that there *had previously been* a waiver. (R. 65)

Although as heretofore stated no issues based upon the motion for new trial or petition for rehearing are properly before this Court, the record shows two other letters written by Attorney Stone, and one by Attorney Hoffmann, which Appellants brought to the attention of Judge Beaumont. From the order denying the motion for new trial and petition for rehearing (R. 102-103) it appears that Judge Beaumont did consider the three additional letters, as it was stated in the order that all evidence, both oral and documentary, filed in the matter was considered.

In the event this Court should determine that it may properly take into consideration these additional letters, Appellees will briefly discuss their effect. Rule 59 (b), Fed. Rules of Civ. Proc., permits a motion for new trial to be made *after ten days* on the sole ground of newly discovered evidence. Regardless of any claimed assurance made to Attorney Shirley, he and his client, who was in court with him, were bound to know what letters had been introduced in evidence. When Attorney Smith agreed that the entire *record* was in evidence, he was referring to everything in the Conciliation Commissioner's official file. This could not mislead the debtor or her attorney into believing that all "off the record" correspondence between her attorney and her creditors was a part of the record. The fact that, when Attorney Carter took over, "he obtained from *Appellants* carbons of two further letters which Mr. Stone sent to Mr. Hoffmann and the original of Mr. Hoffmann's reply of April 9, 1941," does not make the carbons and the letter, *which had been in the hands of his client,* newly discovered evidence.

Newly discovered evidence is material evidence for the

party filing the motion, which he could not, with reasonable diligence, have discovered and produced at the trial. Certainly the three additional letters were available to Attorney Shirley at the time of the trial. Evidently he did not use them because he did not consider them material. No claim is now made that the letters were not available at the time of the trial. The letters might have been new to Attorney Carter, who had just come into the case. To hold that these letters constituted newly discovered evidence would mean that, in order to get a new trial *out of time* in any case, all that would be necessary would be to substitute attorneys and have the new attorney state that he has a new theory of the case under which some additional evidence should have been introduced on behalf of the losing party.

Even if the letters were properly before this Court, there is nothing in them which would militate against Judge Beaumont's conclusions and order. The letter of March 27, 1941, written by Attorney Stone (R. 81) does not indicate any change in Appellants' decision not to file under Subsection (s). The attorney merely informed Appellees that he would notify them when his clients advised him whether they would enter into the agreement; that is, the Possession Agreement that was to be executed by Appellants only in furtherance of their decision "to let the matter go any way that is satisfactory to" Appellees.

The letter of April 3, 1941, from Attorney Stone proves that Appellants were considering only the probability of a settlement with Appellees, de hors the bankruptcy court, in view of the executed contract not to file under Subsection (s). Before signing the Possession Agreement they were exploring the possibility of a scale-down. On April 9, 1941, Appellees' attorney informed them of the impossibility of granting a voluntary scale-down and, therefore, "under the circumstances we feel that the decision made by the debtors . . . is the best solution of the difficulties, and we would like

to have the matter handled as suggested in our last letter," that is, in the way which was most satisfactory to Appellees, under an executed Possession Agreement, so that Appellees could immediately go on the property and protect it from further depreciation, "if Mr. and Mrs. Smith have not changed their minds" about letting "the matter go any way that is satisfactory to" Appellees, *not* about the filing of the petition under Subsection (s).

The whole question of waiver by the debtors is made conclusive, as indicated by Judge Beaumont, by the fact that, after *all* of the correspondence, Florence Davis Smith, the owner of the property, executed the Possession Agreement on May 1, 1941.

On page 13 of their brief Appellants note that the Conciliation Commissioner did not make a finding on the question of waiver, but in the next paragraph they refer to the rule which requires a reviewing court to follow the findings of the trial court unless "entirely erroneous." It is elementary that, where a trial court makes *no* finding on a fact, the reviewing court may and must make its own findings thereon. Therefore, the findings by the District Court on the question of waiver were unquestionably proper.

II.

There Was Adequate Consideration for the Express Waiver

Appellants' third Assignment of Error reads as follows:

> "3. The Court erred in finding that there was a binding agreement to waive the benefits of Subsection (s), since there was no consideration for said alleged agreement."

Appellants contend there was no valid consideration for any waiver agreement. Mr. Avery and the Randolph Marketing Company were permitted to pick the grapefruit crop and

retain all of the proceeds therefrom. The burden of showing a want of consideration lies with the party seeking to invalidate or avoid an instrument. In their brief Appellants state that the point—no consideration—"was made by Mr. Shirley at the hearing on September 3, 1942 (139)." On page 139 of the Transcript of Record it appears that Mr. Shirley stated that he was trying to prove "that there was no consideration for the agreement." This statement, of course, is no *proof* of any *fact*. The only other attempt made by Appellants in their brief to show factual proof of their contention is a reference to a statemnet made by Mrs. Smith (R. 149), and that "Mr. Shirley *stated* that the record showed the Randolph Marketing Company already had the right to market the fruit (R. 149)." Mrs. Smith's statement that "they" gave her no consideration is but a legal conclusion. Attorney Shirley's statement that "it is a matter of record in the court that the Randolph Marketing Company already had the right to market the crop" is not supported by any showing, either before the District Court or this Court. If it was a matter of record, Attorney Carter would certainly not have failed to include it in the one hundred seventy page transcript. Other parts of the record from the Conciliation Commissioner's office were procured by him for inclusion. (R. 91-92)

The record does not contain any order made by the Conciliation Commissioner authorizing the Randolph Marketing Company to make advances which would be repaid from the crop proceeds. No hearing was noticed or held as to the making of such order. No consent thereto was given by Appellees. Even receivers' certificates authorized by a bankruptcy court are not valid unless consented to by lienholders. *L. Maxcy Inc.* v. *Walker,* 119 F.(2d) 535. Under the circumstances, if Appellees had sold the security under a deed of trust before the grapefruit was harvested, the Randolph Marketing Company could not have come upon the property

and picked the grapefruit without the consent requested by Appellants in Attorney Stone's letter of March 21, 1941.

In support of their contention Appellants quote from a case from the Eighth Circuit. (*Buss* v. *Prudential Ins. Co.*, 126 F.(2d) 960, Appellants' Brief 17) The agreement in that case was entirely different. No consideration appeared on the face of the agreement, as in the instant case. Moreover, the quoted portion of the decision shows that lack of a showing of consideration was not the basis for the court's conclusion. The court stated that "There is no showing that the agreement was ever performed by either party to it."

In the instant case there has been full performance of the only demand made by Appellants; that is, the Randolph Marketing Company picked the grapefruit and retained the proceeds.

III

The Waiver Was Made by the Debtors, Not by Their Attorney

Appellants' fourth Assignment of Error reads as follows:

> "4. The Court erred in holding that Attorneys Frederick E. Stone and LeRoy McCormick had power by admissions to waive Appellants' rights to be adjudicated under Subsection (s)."

On page 19 of their brief Appellants cite cases from which it is clear they are attempting to fit the law applicable to one set of facts to an altogether different set of facts. The case at bar is not one where, without the clients' knowledge or authority, the *attorneys* sought to give away certain rights of their clients. A full and complete answer to this contention is the first two sentences in Attorney Stone's letter of March 21, 1941, which read:

> "The matter of filing a petition under subsection (s) has been thoroughly discussed with Mr. and Mrs. Smith,

the above named debtors. *They* have concluded that they will abandon the property and simply let the matter go by default if the Randolph Marketing Company and their agent, Mr. Omer Avery of this city can be protected as to the present grapefruit crop which is now on the trees."

IV

The Right to be Adjudged a Bankrupt Under Section 75(s) May be Waived

Appellants' fifth Assignment of Error reads as follows:

"5. The District Court erred in holding that the rights of Appellants as farmer-debtors to file an Amended Petition under subsection (s) of Section 75 of the Bankruptcy Act could be waived."

The cases from which Appellants quote on pages 20 and 21 of their brief state a rule of law which is not applicable to the facts of the instant case. The courts were considering cases where an agreement to waive the benefits of bankruptcy was demanded by the creditor and incorporated in and as a part of the *original* contract between the parties. This rule of law is analogous to the rule under which a mortgagor may not in the original contract agree to waive his right of redemption. However, it is a rule of universal application that the mortgagor may waive his right of redemption by a subsequent agreement with the mortgagee. For the same reasons a contracting party may not waive the benefits of bankruptcy in the original contract, but may *thereafter* do so by agreement. The *Borchard, Wright, Paradise* and *Corey* cases, cited by Appellants (page 20), are not in point. The *Borchard, Paradise* and *Corey* cases merely hold that, *after a debtor has properly amended under Subsection* (*s*), the statute prescribes an orderly procedure, and that the bankrupt and his creditors can not substitute different procedure from that prescribed in the statute.

In the *Corey* case this Court held that a debtor can not waive the procedure which the statute requires *the Court* to follow.

In the *Wright* case the debtor had not filed an offer of composition or extension, and the court simply held that his right to amend under Subsection (s) did not depend upon the diligence with which he sought to procure a composition or extension.

In the *Trego* case, cited and quoted from by Appellants on page 22 of their brief, the court found that there was *no agreement to waive* any rights under Section 75, and, therefore, any statements made by the court to the effect that an agreement "would have been void as against public policy" is mere dictum.

In the *Morrison* case, cited and quoted from on pages 23 and 24 of Appellants' brief, the mortgagor and mortgagee had agreed that the property should be operated by a receiver. The court held that, regardless of such agreement, "the debtors and creditors could not waive or modify *the provisions* of Section 75." Section 75 (s) (4) expressly provides that "if, at the time that the farmer debtor amends his petition or answer, asking to be adjudged a bankrupt, a receiver is in charge of any of his property, such receiver shall be divested of possession, and the property returned to the possession of such farmer, under the provisions of this title." Naturally the court held that the bankrupt was entitled to possession regardless of the fact that a receiver was in possession prior to the amendment under Subsection (s). There is nothing at all in the case involving the waiver of a right to amend under Subsection (s).

The *Hepker* case, cited and quoted from by Appellants on page 24 of their brief, comes within the rule we have been discussing. The question was whether the mortgagor was

bound to pay rental for a period agreed to by the mortgagor. The court said:

> "We think the statute and not the agreement *made six months before bankruptcy* must control."

The *one case* expressly involving the question of waiver of rights under Subsection (s) is *In re Denney,* 47 F. Supp. 36; 135 F.(2d) 184. This was one of the two cases relied upon by the District Court. (R. 65) The District Court's decision in the *Denney* case was affirmed by the Circuit Court of Appeals. (7th Cir.) Certiorari was denied by the Supreme Court of the United States on October 11, 1943. (64 S. Ct. 50. Rehearing denied November 8, 1943, 64 S. Ct. 155) The *Denney* case is, therefore, the *one final authority* on the question under discussion. The specific question of the validity of a waiver of rights under Section 75(s) was before the court, and in the following language the District Judge expressly held that such rights can be waived:

> "Surely a party litigant may waive his statutory rights, if he does so with full knowledge and has the benefit of competent counsel. Defendants in criminal actions may waive the Constitutional privilege of trial by jury or the right to be arraigned only after the return of an indictment by a grand jury. The Act of Congress known as the Frazier-Lemke Act, 11 U.S.C.A. § 203, was for the benefit of distressed farmers, who, in good faith, were trying to rehabilitate themselves. It was never intended to aid those who, by their acts, in and out of court, attempt to take advantage of its provisions, and give nothing in return. There is no rhyme or reason in holding that the rights extended under this law cannot, under any circumstances be waived."

The Circuit Court held that, while a debtor could not be forced to accept other procedure, as held in the *Borchard* and *Wright* cases, he could agree to waive certain rights, and his agreement was held to be binding. The court rejected

the proposition that a bankrupt is a ward of the court. In the *Denney* case the bankrupt had waived his right to a reappraisal. This is not a prescribed procedural step which is mandatory under the statute. The right to request a reappraisal is *discretionary* with the bankrupt. No cases have been cited by Appellants which hold that a debtor may not waive rights which it is within his discretion to accept or reject.

Section 75 (a-r) was first enacted by the Congress of the United States, and it was specifically provided that the petitioner should be designated "debtor" and not "bankrupt." The purpose of Congress was to provide a procedure under which distressed farmers might procure relief without the stigma of bankruptcy. It is contemplated under Subsection (s) that, if the distressed farmer can not procure the voluntary acceptance of a composition or extension proposal, he may then *elect* to amend his petition and be adjudicated bankrupt. *To hold that it would be against public policy for a debtor who has filed under Section 75 (a-r) to agree for a consideration that he would not become a bankrupt, and that he may not waive his right to be adjudicated bankrupt under Subsection (s) is, in effect, to say that all distressed farmers who file under Subsections (a-r) must ultimately amend under Subsection (s).*

Such an assertion would be tantamount to the contention that every distressed farmer who files under Subsections (a-r) will ultimately be forced to liquidation or to buy the property at the value fixed by appraisers, or by the court. This would prevent any voluntary settlement ever being made with creditors, which is the true purpose of Subsections (a-r). If one who had been adjudicated bankrupt under Subsection (s) felt that he no longer needed the benefits thereof, he would be precluded from filing a voluntary petition for dismissal under Section 59 (g) of the Chandler Act.

If Appellants are correct, it would be necessary for the court to say, upon the filing of a voluntary petition for dismissal:

> "It is against public policy for you to get out of Section 75. You must stay in and either be liquidated or pay *cash* for your property, even though you and all your creditors desire to have the proceedings dismissed."

The District Judge also cited, in support of his opinion, *Cole* v. *Home Owners' Loan Corporation*, 128 F.(2d) 803, a case decided by this Court, wherein it was held that a debtor can waive a right which is for his benefit. In support thereof this Court cited *Boynton* v. *Ball*, 121 U. S. 457, 467. The District Judge also cited many analogous rights which bankrupts have been held to have the right to waive. (R. 67)

V

The District Court's Order Is Sustainable on Grounds Other Than Waiver

The District Court's order of September 17, 1943, was that the property which is security for deeds of trust held by Appellees be stricken from the debtors' schedules, and that Appellees may proceed to have the power of sale in one or both of the deeds of trust exercised in accordance with the laws of the State of California. The order was based upon the fact that the debtors had waived their right to amend under Subsection (s). This was only one of the five separate grounds urged by Appellees for a reversal of the Conciliation Commissioner's order, as set forth in the Points and Authorities filed with the District Court. Reference to said five points was made by the District Judge in his Memorandum Opinion and Order. (R. 64) Where an order grants to a party the relief requested by him, he naturally would not appeal therefrom merely because the decision of the District Court was based upon but one of the several grounds, and the other alleged grounds were held to be insufficient. However,

upon the taking of an appeal by the adversary, the Appellee may in the Circuit Court again assert the additional grounds upon which the order might properly have been predicated, without cross-assignments and without cross-appeal. This rule of law was recognized by the Supreme Court of the United States in *United States, et al.* v. *American Railway Express Co., et al.,* 44 S. Ct. 560, 564, wherein, speaking through Mr. Justice Brandeis, the following statement was made:

> "The Southeastern insists that these claims, although adequately presented in the bill of complaint, cannot be availed of in this court, because they were overruled by the District Court and the American did not take a cross-appeal. The objection is unsound. It is true that a party who does not appeal from a final decree of the trial court cannot be heard in opposition thereto when the case is brought here by the appeal of the adverse party. In other words, the appellee may not attack the decree with a view either to enlarging his own rights thereunder or of lessening the rights of his adversary, whether what he seeks is to correct an error or to supplement the decree with respect to a matter not dealt with below. But it is likewise settled that the appellee may, without taking a cross-appeal, urge in support of a decree any matter appearing in the record, although his argument may involve an attack upon the reasoning of the lower court or an insistence upon matter overlooked or ignored by it. By the claims now in question, the American does not attack in any respect, the decree entered below. It merely asserts additional grounds why the decree should be affirmed. These grounds will be examined."

This rule was also followed and, in fact, quoted by the Supreme Court in *Langnes* v. *Green,* 51 S. Ct. 243, 246, in an opinion delivered by Mr. Justice Sutherland.

Accordingly, Appellees again advance in this Court the arguments presented in the District Court on the additional

four grounds, on any one of which Appellees believe the order of the District Court may *and should be* affirmed.

VI

After the Expiration of a Voluntary Extension Proposal a Debtor May Not Become Aggrieved at It and Amend Under Subsection (s)

Section 75 (s) reads in part as follows:

> "Any farmer failing to obtain the acceptance of a majority in number and amount of all creditors whose claims are affected by a composition and/or extension proposal, or if he feels aggrieved by the composition and/or extension, may amend his petition or answer, asking to be adjudged a bankrupt."

It is not clear whether the debtor may feel aggrieved only *prior to* the confirmation of the composition or extension, or whether he may feel aggrieved *during* the period of an extension, or *after* the expiration of an extension. Since the provision is ambiguous as to when a debtor may feel aggrieved, the Court is forced to resort to well-established rules for determining the proper construction, and should therefore consider the history of the legislation, the legislative intention as indicated by statements made on behalf of the bill by its sponsors in the House and Senate, the legislative intention as indicated by similar legislation, the legislative intention as indicated by the Section as a whole, and as indicated by judicial construction.

A. History of the Legislation

Section 75 (a-r), known as the Debtor's Relief Act, became a law on March 3, 1933. It was then, as it is now, strictly emergency legislation. By its own terms it was to be in effect but five years. At the time of its enactment the United States was in one of its worst economic depressions.

In construing the provision under consideration the Court should consider the facts in retrospect, i.e., as they were when the legislation was enacted, rather than as they are at present. At that time Congress evidently assumed that the economic depression would be over before March 3, 1938. The legislators purposely avoided an adjudication in bankruptcy so that the farmer-debtors would not be faced with the stigma of bankruptcy. Any relief which the debtor might receive depended upon the voluntary action of a majority of his creditors in number and amount.

The sponsors of the legislation soon found that the farmer-debtors were receiving very little relief under this voluntary plan. Accordingly, they set out to put teeth into the Act so that there would be an incentive on the part of creditors to agree to a voluntary composition or extension. Congress, still feeling that relief without the stigma of bankruptcy was desirable, enacted the first Subsection (s), under which a debtor, whose creditors would not cooperate, although being forced to resort to bankruptcy, would nevertheless have five years in which to refinance. This amendment, which constituted the first Subsection (s) and the first Frazier-Lemke Act was later held to be unconstitutional.

Thereafter Congress enacted the present Frazier-Lemke Act. It became a law on August 28, 1935, and provided for a three-year stay. Had it not still been felt that a voluntary composition or extension was preferable, if it could be obtained by voluntary act of the creditors, it seems that Congress would have discarded the voluntary feature incorporated in Subsections (a-r) and merely provided for bankruptcy with the three-year moratorium. However, it must be borne in mind that under Subsection (s) a farmer-debtor must refinance within three years or he loses his farm, as well as all other non-exempt property. Since Congress assumed that the depression would be over by 1938, it very naturally assumed that the farmer-debtors would be able to save their

farms through voluntary extensions under Subsections (a-r), now that it had given the creditors an incentive to grant voluntary extensions rather than force the farmer-debtors to amend under Subsection (s).

When the second Subsection (s) was enacted, on August 28, 1935, several of the prior subsections were amended. This is further proof of the fact that Congress felt that the original purpose of The Deptor's Relief Act, that is, a composition or extension without the stigma of bankruptcy, was still desirable. It would certainly be a reflection on the intelligence of the legislators to conclude that they believed a debtor would be able to procure a *voluntary* extension from his creditors, and, *upon the expiration thereof,* amend under Subsection (s) and procure an *additional* three-year moratorium. The members of Congress would know that the creditors would not grant a voluntary extension if they knew that upon its expiration the three-year stay under Subsection (s) could be *forced* upon them. Congress would be bound to realize that, by making the relief under Subsection (s) absolute, it would be nullifying the whole effect of Subsections (a-r), and would be forcing all distressed farmer-debtors to be adjudicated bankrupts under Subsection (s). With this knowledge, it would not have bothered to amend the several subsections which provide for the debtors' relief under Subsections (a-r).

It is fundamental that, if possible, a statute will be construed by the courts so as to give meaning and effect to each and every part thereof. Should the courts hold that a debtor may procure the full benefits of a *voluntary* extension from his creditors and after the expiration thereof amend under Subsection (s) and procure the full benefits of an *enforced* extension, the result would be to deprive farmer-debtors of the right to effect compositions or extensions without the stigma of bankruptcy, as such a ruling would surely result in the refusal of all creditors to give any consideration what-

soever to offers under Subsections (a-r). As previously stated, the facts should be viewed in retrospect. Suppose this question had been presented to the courts shortly after the second Frazier-Lemke Act went into effect in 1935. It is inconceivable that a court would then have handed down a decision which would have wholly nullified the effect, and deprived the farmer-debtors, of what Congress clearly intended to be the preferable relief. In considering the question at this time a court might easily lose sight of the fact that there was a depression, and that many farmer-debtors saved their farms under Subsections (a-r) where they would certainly have lost them under Subsection (s).

Mr. Justice Douglas, in *Wright* v. *Union Central Life Insurance Co.*, 311 U. S. 273, 61 S. Ct. 196, said:

> "The Act must be liberally construed to give the debtor the full measure of the relief afforded by Congress (John Hancock Mutual Life Ins. Co. v. Bartels, supra; Kalb v. Feuerstein, supra), lest its benefits be frittered away by narrow formalistic interpretations which disregard the spirit and the letter of the Act."

It is submitted that the benefits of Subsections (a-r) will be thus "frittered away" if the relief under Subsection (s) is held to be absolute and cumulative.

B. Legislative Intention as Indicated by Committee Reports and Statements in Congress Pertaining to the First Frazier-Lemke Act

The report of the Committee on the Judiciary and the statements made in Congress when the original Section 75 (s) was being considered, shed significant light on the question as to whether Congress intended that a farmer-debtor should have the full benefits of a voluntary composition or extension under Subsections (a-r), and after the expiration of such extension should then have the full benefits of Subsec-

tion (s). In speaking on behalf of the Bill, *Representative Jones, (Texas)* said:

> "The real compulsory feature of the bill is to the effect that *if* the lien holder and the owner of the land *cannot agree on a program as set out in the bill* (75-*a*-*r*), or some other program, *then* the owner of the land has the right to appeal to the bankruptcy court, and under the control of that court, foreclosure is forbidden for a period of five years, on condition that a reasonable rental be paid during that period . . ." (Cong. Rec. V78, Part 11, Page 12131.)

Representative Lloyd, (Washington) said:

> "By the passage of this act we are simply making workable the bankruptcy act which is already existing law. We are providing a means whereby the farmer may avail himself of an existing law passed by a preceding Congress that was intended to benefit him. (Comment: Unquestionably this refers to The Debtor's Relief Act.)
>
> "Under the law as it now exists, the farmer who cannot pay his debts and avails himself of the bankruptcy act must submit to the rules and regulations laid down by the conciliators appointed. These conciliators may, and often do, in the broad discretionary power conferred on them by the law, make *terms and conditions which the farmers cannot meet*. By this act it is our intent and purpose to provide an honest remedy for the creditor and to provide, too, some method by which the honest farmer . . . may save his home . . ." (Cong. Rec. V78, Part 11, Page 12131.)

Representative Lemke, (North Dakota) co-author said:

> "Therefore I respectfully submit that H. R. 9865 is constitutional, *that in case the debtor and creditor cannot get together and conciliate under Section 75*, it provides an honest and efficient method of scaling down indebtedness . . ." (Cong. Rec. V78, Part 11, Page 12136.)

House of Representatives Report No. 1898, 73rd Congress, Second Session, contains the following statement from the Committee on the Judiciary:

> "In brief the proposed legislation provides that a farmer, *whose efforts under the present agricultural composition section of the bankruptcy act to secure an adjustment of his indebtedness have failed,* may amend his petition, etc. . ."

These statements, by those speaking on behalf of the Bill, and in the Committee reports, clearly show that the purpose of Subsection (s) was to make workable the provisions of Subsections (a-r), under which the debtor could procure relief only if voluntarily agreed to by the majority of his creditors. There were no statements whatsoever indicating a contrary intention. Subsection (s) was considered as a "compulsory" feature, which would give the creditors an incentive to accept a debtor's offer of composition or extension, since the failure to accept such offers would give the debtors the right to amend under Subsection (s) and procure an extension, regardless of the wishes of the creditors. In other words, what Congress intended to do in enacting Subsection (s) was to put some *teeth* in The Debtor's Relief Act.

The first sentence of the original Subsection (s), enacted June 28, 1934, read exactly as does the first sentence of the present Section 75(s), enacted August 28, 1935, and the purpose of the second Subsection (s) is exactly the same as the purpose of the original Subsection (s).

C. Legislative Intention as Indicated by the Present Frazier-Lemke Act

The statements made in Congress on behalf of the second Subsection (s) give no intimation of an intention to make the relief provided therein cumulative to that provided in Subsections (a-r). In fact, three years was expressly provided as sufficient time in which to refinance. If a three-year mora-

torium was considered sufficient for a debtor who *failed* to procure the acceptance of an offer, what reason is there to assume that Congress felt that a debtor who had *succeeded* in procuring a voluntary extension, which might very well have been for three years or more, needed an additional three-year moratorium? It is reasonable to assume that Congress did not intend to grant the debtor, who was *successful* in procuring the acceptance of an offer, substantially more time in which to adjust his affairs than would be available to a debtor who *failed* to procure a voluntary extension.

Again we quote a portion of the provision under consideration:

> "Or if he feels aggrieved by the composition and/or extension, may amend his petition or answer."

Unless Congress intended that the debtor must show good cause for feeling "aggrieved," and unless the courts require such a showing, the word "aggrieved" means nothing, and the sentence would have been worded something like this:

> "*Regardless* of whether a farmer procures the acceptance and full benefits of a composition and/or extension, he may at any time amend his petition or answer, asking to be adjudged a bankrupt and thereupon procure the full benefits of this Subsection."

It is unbelievable that Congress would have set out *two directly opposite* conditions precedent—i.e., if he does, or if he does not procure a voluntary extension—if it intended that the debtor should have the unconditional right to amend at any time.

Considering the provisions from the viewpoint of creditor cooperation, it would be construed in this manner if Appellants' contention is correct:

> "If the creditors of a distressed farmer are *not* coopera-

tive and *refuse to voluntarily grant a three-year extension,* the farmer may be adjudged bankrupt and procure the statutory three-year moratorium *in lieu* thereof, but, if the creditors *are* cooperative and *do grant a voluntary three-year extension,* the debtor may, after the expiration thereof, be adjudicated bankrupt, and procure the statutory three-year moratorium in *addition* thereto."

Such a construction places a premium on non-cooperation and penalizes the creditors who cooperate.

D. Legislative Intention as Indicated by the Express Wording of Subsections (a-r), Considered as a Whole

Several provisions of Section 75 also prove that Congress did not intend that the relief provided for in Subsections (a-r) and the relief provided for in Subsection (s) should be cumulative and consecutive. In fact, they prove an absolutely contrary intention.

Section 75 (c) specifically provides that "at any time prior to (March 4, 1946) a petition may be filed by any farmer, stating that the farmer is insolvent or unable to meet his debts as they mature, and that it desirable *to effect a composition or an extension of time to pay his debts.*"

Subsection (k) provides that a confirmed extension proposal shall be binding on the debtor and his creditors. This means that the proposal becomes a binding contract between the parties.

Subsection (o) provides that certain actions shall not be instituted or maintained against the debtor "at any time *after* the filing of the petition under this section *and prior to the confirmation* or other disposition of the composition or extension proposal by this court."

Subsection (l) provides that upon the confirmation of an

extension proposal, the court may dismiss the proceedings "or retain jurisdiction of the farmer and his property *during the period of the extension* in order to protect and preserve the estate *and enforce through the conciliation commissioner the terms of the extension proposal.*"

These subsections show that Congress had in mind a very definite plan under which a farmer-debtor files a petition for the purpose of *effecting* a composition or extension of his debts, and, after he has succeeded in his purpose, Subsection (k) makes the extension proposal a binding agreement between the debtor and his creditors. In other words, this agreement is substituted, in so far as applicable, for the original agreements between the debtor and his creditors. The automatic stay under Subsection (o) ceases upon "the confirmation or other disposition of the composition or extension proposal by the court." The reason for this is very apparent, as the intention was to provide an automatic stay—Subsection (o)—to afford the debtor an opportunity "to effect a composition or extension"—Subsection (c)—which would become the binding and substituted agreement after confirmation by the court—Subsection (k). After such binding agreement had been substituted, Congress felt that the parties would then carry on under the new agreement, and that there was no need for the further automatic stay.

Congress further provided in Subsection (l) that, upon the confirmation of an extension proposal the court might dismiss the proceedings or retain jurisdiction "*during the period of the extension in order to protect and preserve the estate and enforce* through the conciliation commissioner *the terms of the extension proposal.*" It will be noted that jurisdiction was only to be retained *during the period of the extension* and then *solely* for the benefit of the creditors. Section 75 contains absolutely no provision for retaining jurisdiction after the confirmation of a proposal, except "*during the period of the extension,*" and no provision what-

soever for retaining jurisdiction *after* the period of the extension expires. The express wording of these subsections makes it absolutely certain that Congress did not intend that a debtor could *amend* a petition *after* the court's jurisdiction thereunder had ceased. The provision of Subsection (s) is that the debtor may "amend his petition." This contemplates that there will be a *pending* petition. As the Act does not provide that the court shall retain jurisdiction after the extension expires, it follows that there should be no petition to *amend* after a voluntary extension has expired.

There is additional proof of this in the express words of Subsection (l), which are as follows:

> "The court may, after hearing and for good cause shown, *at any time during the period covered by an extension proposal that has been confirmed by the court,* set the same aside, *reinstate the case* and modify the terms of the extension proposal."

Here Congress provided for the reinstatement of a case which had been dismissed upon the confirmation of the extension proposal, but this right to reinstate exists only "*during the period covered by an extension proposal.*" Very definitely Congress gave the bankruptcy court control by reinstatement only *during the period of the extension.* No right to reinstate *after* the extension expires is provided in the Section.

E. Judicial Construction

The Conciliation Commissioner and the District Judge each appear to have believed that, by reason of this Court's decision in *Cohan* v. *Elder,* 118 F.(2d) 850, he was bound to hold against Appellees' contention on the point under consideration. Appellees do not understand this Court to have held that Congress intended that a debtor should be entitled to the benefits of Subsection (s) whether or not he has re-

ceived the *full* benefit of a voluntary extension. In the *Elder* case the extension had *not expired,* and, therefore, the decision is not authority for the proposition that a debtor may amend *after* an extension proposal has terminated. This Court held that, *if a debtor finds that he is unable to carry out the terms of an extension proposal which he submits and which is confirmed,* he may feel aggrieved and amend under Subsection (s). The decision is very defiite on this point, as the Court said:

> "Congress apparently anticipated that a plan might prove unworkable *upon a trial of it* and therefore provided for an adjudication on petition of the aggrieved debtor notwithstanding the acceptance and confirmation of his own proposal."

The fact that a debtor might find the terms of a voluntary extension too burdensome for him to fulfill and therefore "upon a trial of it" should find it unworkable and should be aggrieved at it is a reasonable and sensible construction of the provision.

The United States Supreme Court has thrice had occasion to refer to the rights of a debtor under the two procedures, although it has not had under consideration the exact question here presented. In *Louisville Joint Stock Land Bank* v. *Radford,* 295 U. S. 555; 55 S. Ct. 854, Mr. Justice Brandeis said:

> "That Act provides, among other things, that a farmer who has *failed* to obtain the consents requisite to a composition under §75 of the Bankruptcy Act, may, upon being adjudged a bankrupt, acquire alternative options in respect to mortgaged property."

In *Adair* v. *Bank of America,* 303 U. S. 350; 58 S. Ct. 594, Mr. Justice Reed said:

> "Upon *failure* of composition and extension, further opportunity for rehabilitation is afforded the debtor,

through provisions enabling him to retain possession of his property, under conditions favorable to its ultimate redemption by him. These steps are carried out under judicial supervision, subsection (s)."

In *John Hancock Mutual Life Insurance Company* v. *Bartels,* 308 U. S. 180; 60 S. Ct. 221, speaking through Mr. Chief Justice Hughes, the United States Supreme Court said:

"Subsection s of Section 75 as amended by the Act of August 28, 1935, prescribed a definite course of procedure. That subsection applies explicitly to a case of a farmer who has *failed* to obtain the acceptance of a majority in number and amount of all creditors whose claims are affected by a proposal for a composition or an extension of time to pay his debts. That was Bartels' situation. Provisions for proceedings by a farmer to obtain a composition or extension, when he is insolvent or unable to pay his debts as they mature, are found in subsections a to r of Section 75, 11 U.S.C.A. § 203, subs. a to r. . . According to the report of the conciliation commissioner, to whom the matter was referred according to the statute, Bartels had appeared at the meeting of the creditors and had submitted to a detailed examination concerning his financial condition . . . He succeeded in obtaining an agreement with certain unsecured creditors for an extension but the secured creditor refused consent, as Bartels could not meet all his arrears. Bartels was thus precisely in the condition prescribed in subsection s . . .

"The plain purpose of Section 75 was to afford relief to such debtors who found themselves in economic distress however severe, by giving them the chance to seek an agreement with their creditors, subsections a to r, and, *failing this,* to ask for the other relief afforded by subsection s."

In *Harris* v. *Zion Savings Bank and Trust Company,* 63 S. Ct. 354, Mr. Justice Douglas, in a dissenting opinion in which Mr. Justice Black and Mr. Justice Murphy joined, and

in which said Justices contended for a broader interpretation for the benefit of farmer-debtors than was conceded, said:

> "The offer of composition made by the decedent before her death might or might not have been accepted. But even though it were rejected, Subsection (s) affords an *alternative* form of relief, one benefit of which is discharge."

From these three decisions it is very evident that the United States Supreme Court has considered Subsection (s) as *alternative* relief rather than as *cumulative* relief. There are no appellate court cases wherein the courts have indicated, even by dictum, that the relief is cumulative.

Because it appears to be a rather general understanding on the part of debtors, creditors, conciliation commissioners, and the District Courts in the Ninth Circuit, that the *Elder* case is authority for the proposition that debtors, who have received the full benefits of Subsections (a-r), may, after the expiration of the voluntary extension, wait until some creditor takes an affirmative step to terminate the matter, and thereupon amend under Subsection (s), Appellees are particularly desirous of procuring a decision herein which will clarify for debtors and creditors, as well as for conciliation commissioners and District Courts in the Ninth Circuit, the effect of the *Elder* case. The instant case affords an excellent opportunity to definitely determine on pertinent facts whether the *Elder* case, which was based upon facts that would make the construction placed placed upon it by the Conciliation Commissioner and the District Judge in this case only dictum, shall be the guide by which creditors decide whether to grant voluntary extensions, or, realizing that the Subsection (s) procedure will be available even after such extension expires, refuse to grant a voluntary extension and force the debtors under Subsection (s) without the additional delay.

VII

The Debtors Procured the Full Consideration to Which They Were Entitled Under Their Extension Proposal, and It Is a Cardinal Maxim of Equity that He Who Takes the Benefit Must Bear the Burden

If we consider in the instant case what the debtors received under their extension proposal, the conclusion that they could not be aggrieved thereby, factually or legally, becomes exceedingly obvious. Without the petition under Section 75, their property might have been sold under the terms of their deeds of trust years ago. The purchasers would thereupon have been entitled to possession. However, because of the voluntary extension granted by the creditors, the debtors have been permitted to retain possession of their property for many years. Their right to retain possession under the proposal ended November 2, 1940, if not earlier, because of defaults. Therefore, according to Subsection (k), there was a binding agreement under which the maximum consideration running to the debtors was possession until November 2, 1940. The binding agreement resulting from the confirmed proposal was, in effect, a lease. The debtors were in the position of a tenant who has had full possession under a lease, and, after the expiration thereof, seeks to have it rescinded on the ground that he, *the tenant*, failed to pay the rental. Under such circumstances it is impossible to see how the tenant could have become aggrieved *after* the expiration of his lease.

In the extension agreement it was contemplated that substantial payments would be made to these Appellees during the three-year voluntary stay. As a matter of fact, not one cent was paid thereunder to Appellees. The debtors, therefore, received everything they bargained for, but Appellees received nothing. Can there be any possible merit to the debtors' contention that *they* are the ones aggrieved at the extension? One needs but very little experience with human

nature to know that a man often feels aggrieved by his burdens, *but not by his benefits.*

It would be contrary to any law of contracts that has yet been advanced if it should be held that a debtor may enter into a binding contract or extension,—Subsection (k)—*procure the full benefits thereof,* and thereafter become aggrieved at what he had received and rescind the contract without returning the consideration, which, in this case, was the extension he received, which can not be returned.

If we consider what a debtor can procure under Subsections (a-r), the fact that *only alternative* relief was intended under Subsection (s) becomes a logical certainty. Subsection (k), as amended on August 28, 1935, permits the reduction of liens to the fair and reasonable market value of the property, and unlimited reduction of interest. Now, let us consider a below-the-average farmer with plenty of debts, who, during prosperous times, borrowed most of the money to purchase a farm. (It could be that he borrowed the life insurance money from a widow with several minor children, and interest on this money was their only source of income.) Along comes a depression, with farm values greatly depressed. The farmer files under Section 75. His other debts constitute a majority in number and amount. He asks for a five-year extension, *and that the lien be reduced to one-half of the secured debt,* which, at the time, may represent the market value of the farm—since there is no market for any farms. He offers to pay one-half of one per cent interest on the reduced amount each year. The offer is accepted by a majority of creditors in number and amount, exclusive of the secured creditor, and confirmed. The debtor would be within his legal rights to retain possession for five years, and the debt would be legally reduced to one-half the amount he borrowed. Would any court believe a debtor who claimed to be aggrieved at such an extension?

Subsection (s) provides for the amended petition if the farmer "feels aggrieved by the *composition* and/or extension." If a debtor may feel aggrieved after an extension expires, he may feel aggrieved *after a composition has been consummated*. The absurdity of permitting him to become aggrieved at a fully executed *extension* proposal is further demonstrated if we consider the effect of his becoming aggrieved at a fully executed *composition*. For example: If a debtor is able to effect a *composition* rather than an *extension* and thereunder pays each creditor, say fifty cents on the dollar, and the composition is confirmed by the court and payment made to each creditor, certainly it would not be held that the debtor might become aggrieved at the composition a few months or years later, require each creditor to refund the payments made to him, and thereupon amend and procure the benefits of Subsection (s). However, the Subsection permits an amendment upon being aggrieved at a *composition* as well as at an *extension*, and there is no more legal basis for holding that he may amend after an extension has been completed than after a composition has been completed.

VIII

If a Debtor Has a Right to Become Aggrieved at an Extension Proposal, the Terms of Which Are Going To Be Too Burdensome for Him To Fulfill, He Must File His Amended Petition Within a Reasonable Time

As provided in Subsection (k), a confirmed extension proposal becomes a binding contract between the debtor and his creditors. This contract supersedes the prior agreement between the parties. The prior agreement was, of course, enforceable under the state law. There is no reason to assume that the substituted contract would not also be enforceable under the state law. The result is that the confirmed extension proposal is governed by the state law, as was the original.

Section 1691, California Civil Code, provides that, when a party desires to rescind a contract, he shall do so *promptly* upon discovering the facts which entitle him to rescind. If a debtor becomes aggrieved at his extension while it is still in effect, that is, if he finds that he will be unable to make the payments which will entitle him to the full extension, he cannot withhold that fact from the creditors, harbor his grievance, accept further benefits under the new contract, (i.e., further extension) and then, when he has received the *full* benefits, make known his grievance and procure what Congress unquestionably intended as alternative relief under Subsection (s). If the statute is properly construed to mean that, if "after a trial," *Cohan* v. *Elder, supra,* the debtor becomes aggrieved at his confirmed extension proposal, he may amend under Subsection (s), it is not necessary to go beyond common sense to determine that he must make his grievance known promptly. There is no other way in which the creditors' rights could be prevented from being "frittered away." A fortiori, if a debtor has the right to amend *after* the expiration of his extension, he must make his grievance known promptly.

In the instant case the extension expired on November 2, 1940. Not a word was heard from the debtors indicating that they felt aggrieved either before or after the expiration. If a proper construction of the Act does not require the debtor to use diligence in manifesting his grievance, the whole burden of the expedient operation of the Act falls upon the creditors. The reason for this would be hard to grasp, but, if true, when a creditor comes into court and asks leave to foreclose, this, at least, should be a signal to the debtor to make up his mind what he wants to do. What else can a creditor do to protect *his* rights? If the present adjudication is allowed to stand, it will likely be a minimum of four years before the moratorium is over. Is the power vested in Congress to pass laws "on the subject of bankruptcies" broad enough to permit a procedure under which a debtor,

in total disregard of the rights of his creditors, may successfully stay the creditors' legal rights for a period of nearly eight years? *In re Wilkins,* 5 F. Supp. 131, Judge Bourquin said in part:

> "... the power to legislate 'on the subject of Bankruptcies' is not power to embrace therein by mere legal label, characterization, form, or forum what is not of, or is foreign to, bankruptcy. Labels, names, go for nothing."

It would seem that the courts should have the power to determine whether the grievance is reasonable or merely a subterfuge for the purpose of obtaining additional relief. If not made known by the debtor until the creditor takes some action to protect his rights, it would appear that the debtor is aggrieved at the attempted interruption of his tranquil and costless possession under the jurisdiction of the bankruptcy court, rather than at the extension, which, as in this case, expired more than a year and a half before the debtors filed their amended petition. Had Appellees waited five years before filing their petition, could the debtors *then* file an amended petition saying they "feel aggrieved" at the extension which expired six and one-half years ago? Neither *Wright* v. *Logan,* 315 U. S. 139; 62 S. Ct. 508, nor *Borchard* v. *California Bank,* 310 U. S. 311; 60 S. Ct. 957, is any authority whatsoever in the present controversy, as in those cases the debtor failed to procure a *voluntary* composition or extension under Section 75 (a-r).

IX

The Conciliation Commissioner's Order of February 9, 1942, Is Not Affected by the Adjudication Under Subsection (s)

Before the debtors filed their amended petition, the Conciliation Commissioner had made and entered an order granting leave to foreclose the deeds of trust held by Appellees. *No appeal was taken from said order.* In *Bernards* v. *Johnson,*

314 U. S. 19; 62 S. Ct. 30, the United States Supreme Court said:

> "The orders and decrees entered by the bankruptcy court, if valid, relieved the respondents, as mortgagees, of any disability to pursue their foreclosure suits arising out of the pendency of the bankruptcy proceeding *and left them free to prosecute the foreclosures in the state courts. However erroneous the challenged orders, the remedy for their correction was by timely appeal.* Since the District Court refused to review these orders and decrees out of time, the petitioners could not attack them in the Circuit Court of Appeals."

Since an order can not be attacked, except by timely review or appeal, it follows that the subsequent adjudication under Subsection (s) did not affect the order of February 9, 1942. A petition under Subsections (a-r) followed, in a proper case, by an amended petition and adjudication under Subsection (s) is but one proceeding in bankruptcy. It is upon the filing of the *original* petition that the bankruptcy court acquires full and exclusive jurisdiction over the debtor and his property. The provisions for this exclusive jurisdiction are in Subsection (n), not Subsection (s). In *Kalb* v. *Feuerstein*, 308 U. S. 433; 60 S. Ct. 343, the United States Supreme Court very clearly established the fact that the exclusive jurisdiction of the bankruptcy court is acquired upon the filing of the *original petition,* and that the injunctions against proceedings in the state court are in Subsections (o) and (p). After quoting from Subsections (n), (o) and (p) the Court said:

> "Thus Congress repeatedly stated its unequivocal purpose to prohibit—*in the absence of consent by the bankruptcy court in which a distressed farmer has a pending petition*—a mortgagee or any court from instituting, or maintaining if already instituted, any proceeding against the farmer to sell under mortgage foreclosure, to confirm such a sale, or to dispossess under it."

In the instant case the bankruptcy court did consent and surrendered its jurisdiction over Appellees' security by the order of February 9, 1942. It had no jurisdiction over said property thereafter, and there is nothing in Subsection (s) which even suggests that an adjudication thereunder brings back to the court jurisdiction previously surrendered. To hold to the contrary would be analogous to holding that, when the bankruptcy court, in general bankruptcy, consents to the foreclosure of a mortgage in a state court, the consent is immediately nullified because the bankrupt still has a justiciable interest in the property.

The District Court held against Appellees on this particular point because of *Brinton* v. *Federal Land Bank of Berkeley,* 129 F.(2d) 740, wherein the Circuit Court of Appeals, Tenth Circuit, held that, although the bankruptcy court had consented to the foreclosure of a mortgage in the state court in an order made while the debtor was under Subsections (a-r), such order had no effect after an amendment under Subsection (s) because the debtor still had a justiciable interest in the property at the time of adjudication. As the Circuit Court of Appeals held in favor of the secured creditor on another point, the above holding was not questioned on appeal. It is submitted, however, that the Circuit Court failed to take into consideration the fact that *proceedings under (a-r) and under Subsection (s) constitute but one proceeding before the bankruptcy court.* When this fact is kept in mind, together with the further fact that an order was made authorizing the secured creditor to proceed with foreclosure in the state court, i.e., consenting that the state court should take jurisdiction, and together with the further fact that there was no review or appeal from the order granting leave to foreclose, it will be seen that to hold that at the time of adjudication under Subsection (s) the debtors had a justiciable interest in the property was wholly beside the point. Such a holding would mean that, if an order was made which under all of the rules of the court had become final

and not subject to either direct or collateral attack, some further step in the proceeding could have the effect of nullifying such order without a rehearing, review, appeal or order setting aside and vacating such order. True, the debtors had a justiciable interest in the property at the time of adjudication. They also had a justiciable interest in the property the day after the order granting leave to foreclose was entered and the day after the final time for review or appeal expired, but a mere justiciable interest in the property under the bankruptcy court's jurisdiction does not have the effect of *nullifying orders* made by the bankruptcy court in respect to such property.

What has just been said is wholly and completely substantiated by the decision in *In re Casaudoumecq,* 46 F. Supp. 718, recently handed down by the United States District Court, Southern District, California, in a case where on March 20, 1942, the mortgagee filed with the court its "petition for leave to enforce chattel mortgage." On March 23, 1942, an order was entered permitting foreclosure of the mortgage, and on May 5, 1942, the debtor was adjudicated bankrupt under Section 75 (s). This is the exact continuity of the orders and adjudication in the instant case. Judge Ralph E. Jenny said:

> "The adjudication of the debtor as a bankrupt under subdivision s of Section 75 came *after the time for appeal from the order* of foreclosure of March 23rd *had elapsed.* What effect did this adjudication have upon that order? *A debtor's proceedings under sub. s are but a continuation of proceedings under the other provisions of Section 75, subs. a-r;* and, if the original petition, as here, was sufficient to show the jurisdiction of the court (particularly that the debtor was a farmer within the meaning of the act), *such jurisdiction continues.* Leonard v. Bennett, 9 Cir., 116 F. 2d 128, 44 A.B.R., N.S. 745; In re Brown, D.C.S.C. Iowa, 21 F. Supp. 935, 36 A.B.R., N.S., 828. In the case of Potter v. Union Central Life Ins. Co., 6 Cir., 111 F. 2d 145, 42 A.B.R., N.S., 880, it was held that the statutory stay of fore-

closure proceedings pending against a debtor's property, provided for in Section 75, sub. o, should not be vacated upon a motion filed by the mortgagee prior to the debtor's adjudication under sub. s, and before the debtor has had any reasonable opportunity to demonstrate the possibility of his rehabilitation within three years under sub. s. However, in the case at bar the stay was vacated by the order of March 23rd, and, *since no motion for a new trial was made, and no appeal taken within the time required, or at all, such order became final, binding and impregnable to subsequent attack, no matter how erroneous* that order may have been. Bernards v. Johnson, 314 U.S. 19, 62 S. Ct. 30, 86 L.Ed. , 47 A.B.R., N.S., 130. *Furthermore, the debtor here has had ample opportunity to demonstrate the possibility of his financial rehabilitation. This he has signally failed to do.* The record shows that, during the more than three years elapsing between the time the proceeding was commenced until the adjudication under sub. s, the debtor's financial condition, instead of improving, has steadily been growing worse, and the value of the bank's security under the chattel mortgage has been steadily depreciating."

"In bankruptcy, a stay of reasonable duration, and the risk naturally accompanying it, may be accepted as an incident of the proceeding, but *creditors must not be subject to irreparable injury by unreasonable suspension of their remedies.* United States Nat'l Bank v. Pamp, 8 Cir., 83 F. 2d 493, 31 A.B.R., N.S., 38; Continental Illinois Bank v. Chicago R.I. & Pac. Ry. Co., 294 U. S. 648, 55 S. Ct. 595, 79 L.Ed. 1110, 27 A.B.R., N.S., 715. Here the bank has been stayed for a period of more than three years, during practically all of which time the debtor has *neglected the estate and ignored his obligation.* It appears from the records before the court that any further stay may, and it is reasonable to assume that it would, result in irreparable injury to the bank as a secured creditor."

"We are not concerned here with the problems that were before the Supreme Court for solution in the cases of Borchard v. California Bank, 310 U. S. 311, 60 S. Ct.

957, 84 L.Ed. 1222, 42 A.B.R., N.S. 596, and Wright v. Union Central Life Ins Co., supra. In those cases it was held error for the lower court, after an adjudication under sub. s, to vacate the stay and permit the secured creditor to foreclose until certain steps were taken under sub. s for the benefit and protection of the debtor. *Here we are dealing with the effect of an adjudication under sub. s, after a vacation of the stay and a decree of foreclosure by the bankruptcy court which became final and conclusive before the debtor's amended petition was filed for adjudication under sub. s.*"

X

The Debtors Are Estopped from Procuring the Benefits of Subsection (s) Insofar as The Federal Land Bank of Berkeley, the Federal Farm Mortgage Corporation and Their Securities are Concerned

Following the hearing on March 21, 1941, the debtors, through their attorney, represented to Appellees that, if the Randolph Marketing Company was permitted to take the grapefruit then growing on the premises, they would abandon the property, let the case go by default, and permit the matter to be terminated in any manner satisfactory to Appellees. By reason of these representations, Appellees were led to believe that following the harvesting of the 1941 grapefruit crop there would be no opposition to foreclosure under their deeds of trust, and, accordingly, permitted the Randolph Marketing Company to harvest said grapefruit crop and retain the proceeds thereof, went into possession of the property under the Possession Agreement signed by Florence D. Smith and the order signed by the Conciliation Commissioner, expended substantial sums in the care and preservation of the property, and made no attempt to bring the question as to the debtors' right to amend under Subsection (s) to an early determination. By reason of the debtors' promises and actions, the stay of proceedings under Subsection (s), if the debtors are entitled to such stay, will begin more than a year later than it would have begun had it not

been for the promises and actions of the debtors. To permit them to procure the benefits of Subsection (s) at this late date would be to reward them, for their lack of good faith, with the possession of their property for an additional year or two without the obligation of paying rental therefor.

In 8 *C.J.S.* 431, the equitable nature of bankruptcy courts is well stated:

> "The court endeavors to do equity whenever possible; it is armed with equity powers in aid of its jurisdiction and the enforcement of its orders; *equitable doctrines and principles prevail therein and are controlling;* and the court will not permit itself to be used for the purpose of perpetrating a fraud or attaining an inequitable result."

The District Judge held against Appellees on the ground that there had been no showing of contumacious acts by Appellants. The word "contumacious" was injected into Section 75(s) by Mr. Justice Douglas in *Wright* v. *Union Central Life Ins. Co.,* 61 S. Ct. 196. However, in doing so the Supreme Court committed an error which has so often been condemned—judicial legislation. The word was read into the last sentence of Section 75(s)(3). A cursory or a studied reading thereof will conclusively prove that Congress did not base the relief therein provided on any *contumacious* act on the part of the debtors. It is plainly and simply provided what may happen, if the debtors fail to comply with the provisions of the section or with the orders of the court.

In conclusion it is respectfully submitted that on several separate grounds the order of the District Court authorizing Appellees to proceed with the enforcement of their liens in the State court should be affirmed.

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Attorneys for Appellees.

No. 10666.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

FLORENCE DAVIS SMITH and HARVEY W. SMITH,
Appellants,

vs.

THE FEDERAL LAND BANK OF BERKELEY and FEDERAL FARM MORTGAGE CORPORATION,
Appellees.

APPELLANTS' REPLY BRIEF.

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Appellees.

APPELLANTS' REPLY BRIEF.

Jurisdiction.

Appellees claim that there can be no motion for new trial before the District Court and that the Order denying the Petition for Rehearing is not appealable. (Appellees' Br. pp. 2-3.) Appellants' Petition, filed on October 16, 1943, asked for a new trial, a rehearing and a motion to vacate the judgment. It was accompanied by the Affidavit of Appellants' own counsel setting forth three additional letters between Mr. Stone and Mr. Hoffman bearing on the question of waiver and asking that the case be re-opened for the consideration of these documents and to permit further oral testimony which was excluded at the hearing before the Conciliation Commissioner on September 3, 1942. [R. 74-83.]

Judge Beaumont, on October 16th, 1943, entered an Order stating that the Motion for New Trial, Petition for Rehearing and Motion to Vacate the Judgment had been seasonably presented and entertained. [R. 78.]

It is well settled that a District Judge on reviewing an Order of a Conciliation Commissioner, has the authority to consider additional evidence, and that he does not sit as an ordinary reviewing court.

Dunsdon v. Federal Land Bank, 137 Fed. (2d) 84.

It was Judge Beaumont's duty to reopen the case on one or more of the three types of relief sought in the Petition. Certainly the facts warranted a vacating of the Judgment on the ground of mistake, inadvertence or excusable neglect. (Rule 60, Federal Rules of Civil Procedure.)

I.

There Was No Waiver of the Right to Be Adjudicated Under (s).

In the six pages of Appellees' Brief (pp. 6-11), claiming an express waiver agreement, there is no answer to our claim (Op. Br. pp. 9-11) that conditions were set up in Mr. Hoffmann's reply of March 26, 1941, which were never at any time complied with and so there could never have been any meeting of the minds and therefore no agreement.

Indeed there is not even any comment by Appellees' counsel to the portions of Mr. Hoffmann's letter set out in italics in our Brief (pp. 9-10). Counsel asserts (p. 7), "The debtors withdrew their opposition and consented to the Conciliation Commissioner's order." They cite in

support of this only the Commissioner's Findings in the Order of February 9, 1942. The record shows that the only hearing before the Commissioner was held on March 12, 1941. All of the correspondence between the parties, both that relied on by Judge Beaumont as amounting to a waiver, and the three additional letters relied on by Appellants as showing conclusively that no waiver had been made occurred long after that hearing of March 12th and there is nothing to indicate that any evidence relating to such correspondence came to the attention of the Commissioner. Therefore, if we are correct in our view that the Order of February 9, 1942, was wholly void as not within the power of the Commissioner to enter, there is no evidence in the record to sustain Appellees' position.

We pointed out in our Opening Brief (p. 26), that the Commissioner's Order of February 9, 1942, was void and not voidable. While subdivision (o) of Section 75 contained the phrase "prior to the confirmation or other disposition of the composition or extension proposal," nevertheless, this section has been construed in more recent decisions to control as to matters arising in later proceedings under Section 75. (*Bastian v. Erickson,* 114 Fed. (2d) 338 at 140; *Schriever v. Oxford Building & Loan Ass'n.,* 116 Fed. (2d) 683, at 684.) Moreover, the case of *Bernard v. Johnson,* 314 U. S. 19, 86 L. Ed. 11, 62 S. Ct. 30, declined to pass on this precise question as not being necessary for a decision in that case (86 L. Ed. 20).

Appellees claim that Section 1(9) of the Chandler Act providing that a Referee may act as a Court gave the Conciliation Commissioner authority to enter the Order of February 9, 1942. Since subsection (o) of Section 75 of the Act states that the *"Judge" "must enter an Order,"*

there can be no doubt that any Order by a Commissioner permitting foreclosure entered prior to the confirmation or other disposal of an Extension Proposal would be void. We submit that under the authorities cited above, the same prohibition against the entry of an Order by a Commissioner applies here.

Counsel for Appellees insist (pp. 8-9) that Judge Beaumont held that the Possession Agreement did not constitute a waiver but merely supported his conclusion that there had previously been a waiver. Mrs. Smith's testimony and offers of proof (Appellees' Op. Br. pp. 11-13) clearly show that no such conclusion by the District Judge was justified.

Counsel are in the inconsistent position of stating in one breath that Judge Beaumont took into account the three additional letters set up by the Affidavit supporting the Petition for Rehearing, Motion for New Trial and Motion to Vacate Judgment and yet still insisting that those letters are not properly before this Court on Appeal (Appellees' Br. p. 9.)

It is further claimed that regardless of any claimed assurance made to Mr. Shirley by Mr. Percy Smith, both Mr. Shirley and Mrs. Smith were bound to have known what letters were and were not in evidence. This position is unsound. Mr. Shirley, who admittedly had substituted for another attorney, was justified in relying on Mr. Percy Smith's assurances, particularly since the Commissioner said he would not allow Mr. Shirley time to go

through the record. [R. 163.] Counsel proceed to go outside of the record and insist that these additional letters were available to attorney Shirley and that he did not use them because he did not consider them material. (Appellees' Br. p. 10.) This is not the fact. Present counsel for Appellants was retained on October 7, 1943. [R. 79-81.] The three additional letters between Mr. Stone and Mr. Hoffman were actually not obtained by Appellant, Florence Davis Smith from Mr. Stone until September, 1943, when received under a covering letter from Mr. Stone dated September 19, 1943, the original of which is available for presentation to this court. Mr. Stone there stated that he managed to get one day off from the Navy to make a trip to Porterville to get the papers requested.

Counsel for Appellees assert that Mr. Hoffman in putting in the phrase, "if Mr. and Mrs. Smith have not changed their minds," only meant letting the matter go any way that was satisfactory to Appellees and that he did not mean to refer to the filing of a Petition under subsection (s). Such an argument is entirely untenable since at all times, the principal alternative to letting the matter go by default would be to file under (s).

We submit that on the record, without the three additional letters set up by Affidavit, it is shown there was no waiver. The three later letters confirm the construction that no waiver occurred.

II.

There Was No Consideration for the Alleged Waiver.

Counsel for Appellees insist that there is no evidence in the Record to support Appellants' contention that the Randolph Marketing Company already had the authority to pick the grapefruit and retain the proceeds. They concede that Mrs. Smith did testify that there was no consideration but insist this was only a legal conclusion. (Appellees' Br. p. 10.) At the hearing on September 3, 1942, it was the duty of counsel for Appellees, if they were going to object to Mrs. Smith's statement, to ask to have it stricken as a mere legal conclusion. This they did not do, although at other points at that hearing, the record shows they made that precise objection which was sustained.

In any event there is direct evidence by Mrs. Smith that the Randolph Marketing Company was already handling all of the fruit under an Order of Court which therefore establishes that there was no consideration for the alleged waiver. This testimony [R. 129] is as follows:

> "Q. (By Mr. Shirley): * * * since 1937, when you filed, who has handled the picking and marketing of those crops? A. Randolph Marketing Company has until last November.
>
> Q. Was that pursuant to the order of the Court? A. Yes.
>
> Q. And what happened to the proceeds of those funds? A. They were handled through Randolph Marketing Company, and they were made agents to pay all bills incurred for operation, and * * * with any surplus to pay out on debts."

III.

Neither Mr. Stone nor Mr. McCormick Had Any Power by Admission to Waive the Right of Appellants to Go Under (s).

Appellants insist that cases cited under Point IV of our Opening Brief do not fit the facts in this case and that the language used in Mr. Stone's letter of March 21, 1941, to the effect that they (meaning Appellants) had concluded that they would let the matter go by default if the Randolph Marketing Company could be protected, is a complete answer to our position. On any theory, the letter of March 21, 1941, was not self-executing and at the most it was an offer that had to be accepted. As we have pointed out, it never was accepted but conditions and restrictions were imposed which were never carried out nor agreed to by appellants. Therefore there was no meeting of the minds. This is conclusively shown by the later correspondence.

Appellees have insisted (pp. 8-9) that Mr. McCormick's statement was proof that Appellants had previously waived. Certainly such an attempt to establish a waiver by admission is improper under the authorities cited in our opening brief.

IV.

The Right to Be Adjudicated a Bankrupt Under Subsection (s) Can Not Be Waived.

Appellees claim that the cases relied on by us cover only the invalidity of an agreement to waive the benefits of Bankruptcy where incorporated as a part of an original contract between the parties. They even attempt to distinguish the case of *Hepker v. Equitable Life Assurance Society,* 131 Fed. (2d) 926, on this theory. As pointed out on page 24 of our Opening Brief, the alleged agreement in the *Hepker* case occurred while they were under an (a-r) proceeding just as in our case and when the Circuit Court of Appeals said, "we think the statute and not the agreement made six months before bankruptcy must control," they meant by bankruptcy *going under subsection (s),* the precise point involved in this case.

Nor can the language of the Circuit Court of Appeals in *Trego v. Wright,* 111 Fed. (2d) 990, and *Federal Land Bank v. Morrison,* 133 Fed. (2d) 613, be so lightly brushed aside as counsel attempt.

Counsel quotes at length from *In re Denny,* 135 Fed. (2d) 184 as *the one case* establishing that the right to go under (s) may be waived. In that case the debtor filed an amended petition under subsection (s) and was so adjudicated. The question of waiver arose not on the matter of going under (s) but on whether after an appraisement and an application for reappraisement, the debtors could waive the right to such reappraisement and

make an agreement that the property might be sold if he did not redeem it at a given figure by a set date. This is an entirely different question from whether a debtor while under (a) to (r) can waive his right to file an amended petition under subsection (s).

On page 14, Counsel for Appellees state that the cases of *Borchard v. California Bank,* 310 U. S. 311, 84 L. Ed. 1222, 60 S. Ct. 957; *Wright v. Logan,* 315 U. S. 139, 84 L. Ed. 443, 62 S. Ct. 508, and *Corey v. Blake,* 136 Fed. (2d) 162, "hold that after a debtor has properly amended under subsection (s) the statute prescribes an orderly procedure and that *the bankrupt and his creditors cannot substitute different procedure from that prescribed by the statute.*" (Emphasis ours.) At page 17 of their brief, counsel go on to say: "In the *Denny* case the bankrupt had waived his right to a reappraisal. This is not a prescribed procedural step which is mandatory under the statute."

With these two statements we agree.

The decision of this court in *Cole v. Home Owners Loan Corporation,* 128 Fed. (2d) 803, by a divided court, does not meet the test which Appellees have set up, since the procedure there held to be waived was one prescribed by the statute: but in any event that case is not persuasive on the question of the right to go under (s). The debtors were already under (s).

The claim (bottom of p. 17) that the public policy doctrine against waiver would mean "that every distressed

farmer who files under subsections (a-r) will ultimately be forced to liquidation or to buy the property at the value fixed by appraisers, or by the court" is simply specious. And the further claim that "this would prevent any voluntary settlement being made with creditors" and that one who had been adjudicated under (s) "would be precluded from filing a voluntary petition for dismissal under Section 59 (g) of the Chandler Act" is absurd.

Of course a farmer can make any voluntary settlement with his creditors he may wish, once he has amended his petition under Subsection (s) but he cannot under the holdings of the Supreme Court be deprived of his statutory right to go under (s), either with or without his consent.

After a farmer has filed under (a) to (r) and is attempting to work out an extension or composition agreement he is still in distress and under pressure from his creditors. If under that pressure he can be compelled to forego all right to go under (s), the whole of Section 75 would be largely made valueless. We respectfully submit that it would be clearly against public policy to hold that a farmer under such compulsion from his creditors could waive his right to be adjudicated a bankrupt under Subsection (s).

V.

Reply to Appellees' Points VI to X.

Appellees assert that the language of Section 75(s) is ambiguous in that it is not clear whether the debtor may feel aggrieved only *prior* to confirmation or whether he may feel aggrieved *during* the period of an extension or *after* the expiration of an extension. (Appellees' Br. p. 20.)

Because of this alleged ambiguity, counsel proceeds in the next ten pages to discuss at some length the history of the legislation generally and as indicated by legislative statements and committee reports.

The answer to all of this argument is that this Court's decision in *Cohan v. Elder,* 118 Fed. (2d) 850, in which certiorari was denied by the United States Supreme Court, 313 U. S. 583, 85 L. Ed. 1539, 61 S. Ct. 1102, held there was no ambiguity. This Court in that case said (page 851):

> "The revelant provision of subsection (s) is that 'any farmer failing to obtain the acceptance of a majority in number and amount of all creditors whose claims are affected by a composition and/or extension proposal, *or if he feels aggrieved by the composition and/or extension,* may amend his petition or answer, asking to be adjudged a bankrupt.' (Emphasis supplied.) In the plainest of language this provision extends to the debtor, as of right, the relief given him below. Compare *John Hancock Insurance Co. v. Bartels,* 308 U. S. 180, 60 S. Ct. 221, 84 L. Ed. 176."

On page 32 of Appellees' Brief, they rather naively concede that "it appears to be a rather general understanding on the part of debtors, creditors, conciliation

commissioners, and the District Courts in the Ninth Circuit, that the *Elder* case is authority for the proposition that debtors, who have received the full benefits of Subsection (a-r), may, after the expiration of the voluntary extension, wait until some creditor takes an affirmative step to terminate the matter, and thereupon amend under Subsection (s), . . ."

We respectfully submit that the reason all of these various groups have reached that "general understanding" is that most, if not all, of the arguments presented by Appellees in this case were presented to this Court by counsel for *Cohan* in the *Elder* case and overruled.

At page 31 of their brief in this case, counsel refer to the decision in *John Hancock Mutual Life Insurance Co. v. Bartels,* 308 U. S. 180, 84 L. Ed. 176, 60 S. Ct. 221, making a long quotation from it including the paragraph as to the purpose of Section 75 being to give debtors "the chance to seek an agreement with their creditors, subsections a to r, and, *failing this,* to ask for the other relief afforded by subsection s."

This very passage was quoted at page 15 of Appellants' Opening Brief in this court in the *Elder* case and again at page 5 of the Reply Brief. It was again quoted in Cohan's Petition for Certiorari filed in the Supreme Court of the United States.

The undersigned prepared the Elder briefs in *Cohan v. Elder,* and there pointed out that in the *Bartels'* case the Court was talking about the two ordinary alternatives which arise, namely, an agreement under a to r or the filing of a petition for relief under subsection (s). The court did not have before it any necessity for construing the

language of a farmer debtor feeling aggrieved by the composition or extension. To interpret the language of the *Bartels'* case as covering every possible contingency would render that portion of subsection (s) relating to a farmer feeling aggrieved by a plan absolutely meaningless.

Appellees claim that since Appellants received a three-year stay and had fallen down on the payments under the proposed plan they could not be aggrieved factually or legally by the plan. (Appellees' Br. p. 33.)

The Record filed in this Court in the *Elder* case showed that on July 2, 1940, Cohan, the principal secured creditor, filed a Petition in the District Court for leave to sell the twenty acres on which Cohan held a trust deed, on the ground that the Elders had been unable to comply with the confirmed plan as modified and had failed to secure rehabilitation. [Cohan v. Elder, R. 66.] A supporting Affidavit alleged that one year's interest and $2500 of principal were delinquent on the Cohan obligation and that current obligations were unpaid and principal obligations delinquent of more than $13,000. [Cohan v. Elder, R. 67.]

The following day, July 3, 1940, the Elders asked to amend under (s). The Commissioner recommended that they be adjudicated under (s) and the adjudication followed on July 5, 1940. [Cohan v. Elder, R. 62.]

In the *Elder* case, the original petitions for relief under Section 75 were filed in the District Court on July 13, 1937. [Cohan v. Elder, R. 18, 21.] The extension proposal plan, after approval by a majority of creditors, was filed on September 30, 1937 [Cohan v. Elder, R. 21] and confirmed by the Court on May 24, 1938. [Cohan v. Elder,

R. 24.] In September, 1939, the plan was modified by the Court reducing the rate of interest and postponing certain principal payments. [Cohan v. Elder, R. 45.] On appeal to this Court that action was affirmed on June 7, 1940. (112 Fed. (2d) 967.) The adjudications under (s) of July 5, 1940, were sustained on July 15, 1940, by the District Court and that action afterward affirmed by this Court. Under those rulings the Elders were given to and including three more years from whatever date the three-year stay order under (s) was entered and rental fixed, within which to rehabilitate or refinance themselves which would have given them a total of some seven or more years from the time they filed their original petition.

Here again we have identically the same argument advanced in the *Elder* case where the Petition to set aside the adjudication under (s) alleged that "the debtors have had a plan of composition and extension in operation for approximately thirty-three months and have miserably failed to comply with the terms thereunder or as modified by the Court." [Cohan v. Elder, R. 71.]

Furthermore, the case of *Brinton v. Federal Land Bank,* 129 Fed. (2d) 790, cited by Judge Beaumont in his Memorandum Opinion carried the *Elder* case one step further. It held that the property there in question had been discharged from the proceedings under (a-r) by a failure by the debtor for more than three years to even file any offer of composition or extension. The upper court therefore justified the District Judge in having entered an Order authorizing the mortgagee to foreclose. Four months later the debtor filed under subsection (s), thus presenting an almost identical situation with the present

case and Appellees' claim regarding the Commissioner's Order of February 9, 1942, except that in the *Brinton* case, the Order was properly entered by the District Judge and not by the Commissioner who, as we maintain, had no power to enter such an Order. The Circuit Court of Appeals of the Tenth Circuit went on in the *Brinton* case to hold that so long as the mortgagee had not in that intervening four months, completed its foreclosure, the debtor still had a justiciable interest in the property which the Bankruptcy Court continued to have power to administer. This is precisely the situation in our case.

It is further argued (p. 35) that if a farmer considers himself aggrieved "he must file his amended petition within a reasonable time."

This precise point was made in the *Elder* case and this Court disposed of it at page 851 in the following language:

> "Appellant argues, in the alternative, that the court was without jurisdiction to order an adjudication because the amended petition was not made within a reasonable time after confirmation. We see no merit in the argument. The statute says nothing about a reasonable time. The act is to be construed liberally to accord the debtor the full measure of the relief afforded by Congress. *Wright v. Union Central Life Insurance Company,* 304 U. S. 502, 58 S. Ct. 1025, 82 L. Ed. 1490."

This same point was later presented to and overruled by the Supreme Court in *Wright v. Logan,* 315 U. S. 139, 86 L. Ed. 745, 62 S. Ct. 508.

Judge Beaumont was justified in disregarding the Commissioner's Order under authority of *Brinton v. Federal Land Bank,* 129 Fed. (2d) 740. Appellees argue that

the Court of Appeals in that case failed to recognize that proceedings under (a-r) and under (s) constitute but one proceeding in Bankruptcy. We do not agree. As pointed out in the case of *Klevmoen v. Farm Credit Administration,* 138 Fed. (2d) 608, at 611, the object as well as the procedure in farm debtor cases is entirely different from that in ordinary bankruptcy. Therefore, since the act of going under (s) is most nearly similar to ordinary bankruptcy the cases set out at pages 20 and following of our Opening Brief clearly support the decision in the *Brinton* case.

In the case of *In re Casaudoumecq,* 46 Fed. Supp. 718 (Appellees' Brief p. 40) Judge Jenney reaches a result squarely in conflict with that arrived at by the Circuit Court of Appeals in the *Brinton* case and also in conflict with Judge Jenney's own decision in the case of *In re Los Angeles Lumber Products Co., Ltd.,* 24 Supp. 501, quoted at page 21 of our original Brief.

Appellees claim that Appellants, by their conduct, misled Appellees so that they made no attempt to bring the right of Appellants "to amend under subsection (s) to an early determination". Mrs. Smith's testimony and offers of proof [R. 141-145, 154-155] show that throughout the period in question, negotiations were going on between the parties looking to some amicable arrangement whereby Appellants' interest could be protected without having to file an amended petition under (s). On this state of the Record there can be no estoppel pleaded against Appellants.

Judge Beaumont held that Appellants were not guilty of "contumacious" conduct, and he was clearly right in so doing. The holding in *Wright v. Union Central Life In-*

surance Co., 311 U. S. 273, 85 L. Ed. 184, 61 S. Ct. 196, that "contumacious" conduct is necessary before a debtor's rights can be cut off, is still the law and is being followed by Circuit Courts of Appeals:

Peterson v. John Hancock Mut. Life Ins. Co., 137 Fed. (2d) 396.

If the doctrine of estoppel and of coming into equity with clean hands, should be applied to either side in this case, it should be invoked against Appellees.

Conclusion.

The Record in this case demonstrates that Appellants never intended to waive their rights under Subsection (s) and that no waiver was in fact made. Even if there had been a formal valid waiver made in writing in open court, such waiver would have been void as against public policy.

More than one-half of Appellees' entire brief (pp. 20 to 43, both inclusive), is nothing more than an attempt to persuade this Court to reverse its holding in the case of *Cohan v. Elder,* 118 Fed. (2d) 850, as well as the two chief cases in which the *Elder* case was followed, namely, the Supreme Court decision in *Wright v. Logan,* 315 U. S. 139, and *Brinton v. Federal Land Bank,* 129 Fed. (2d) 740. We therefore urge that Judge Beaumont's Order of September 17, 1943, should be reversed and the proceedings under subsection (s) be permitted to go forward.

Respectfully submitted,

ALLAN J. CARTER,

Attorney for Appellants.

No. 10697

United States
Circuit Court of Appeals
For the Ninth Circuit.

AMELIA DAVIS BLOCH,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Transcript of the Record

Upon Petition to Review a Decision of the Tax Court of the United States

Rotary Colorprint, 590 Folsom St., San Francisco

No. 10697

United States
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AMELIA DAVIS BLOCH,

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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APPEARANCES:

For Taxpayer:

W. H. ORRICK, Esq.,
CHAS. L. BARNARD, Esq.,

For Comm'r:

HARRY R. HORROW, Esq.,

Docket No. 112225

AMELIA DAVIS BLOCH,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1942

Aug. 21—Petition received and filed. Taxpayer notified. Fee paid.

Aug. 22—Copy of petition served on General Counsel.

Sept. 16—Answer filed by General Counsel.

Sept. 16—Request for Circuit hearing in San Francisco, Calif. filed by General Counsel.

Sept. 22—Notice issued placing proceeding on San Francisco, Calif. calendar. Service of answer and request made.

1943

Jan. 5—Hearing set Feb. 1, 1943, San Francisco, Calif.

1943

Feb. 1—Hearing had before Judge Smith on the merits. Consolidated. Stipulation of facts filed. Petitioner's brief due 3-20-43. Respondent's brief due 4-20-43. Reply brief due May 5, 1943.

Feb. 24—Transcript of hearing 2-1-43 filed.

Mar. 20—Brief filed by taxpayer. 3-20-43 Copy served on General Counsel.

Mar. 20—Stipulation for correction of transcript filed.

Apr. 20—Reply brief filed by General Counsel.

Apr. 29—Order extending time to June 4, 1943 to file reply brief entered.

May 31—Order extending time to July 6, 1943 to file reply brief entered.

July 5—Reply brief filed by taxpayer. 7-5-43 Copy served on General Counsel.

Aug. 14—Memorandum opinion rendered, Smith, Judge, Div. 5. Decision will be entered under Rule 50. 8-16-43 Copy served.

Sept. 2—Computation filed by General Counsel.

Sept. 4—Notice of hearing 10-6-43 under Rule 50.

Oct. 2—Consent to settlement filed by taxpayer.

Oct. 5—Decision entered, Smith, Judge, Div. 5.

1944

Jan. 3—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, filed by taxpayer.

Jan. 11—Affidavit of service by mail filed by taxpayer.

Feb. 1—Praecipe for record filed by taxpayer and affidavit of service by mail.

1944

Feb. 12—Certified copy of an order from 9th Circuit extending the time to 3-11-44 to prepare and transmit the record filed.

Feb. 14—Affidavit of service of petition for review filed.

Feb. 14—Affidavit of service of the above order from Circuit Court to J. P. Wenchel filed.

[1*]

United States Board of Tax Appeals

Docket No. 112225

AMELIA DAVIS BLOCH,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Bureau symbols IRA:90-D-WHL (C:TS:PD-SF:WGW)) dated May 26, 1942, and as the basis of her proceeding alleges as follows:

I

The petitioner is an individual whose mailing address is 343 Sansome Street, San Francisco, Cali-

*Page numbering appearing at top of page of original certified Transcript of Record.

fornia, and whose residence is 20 Cherry Street, San Francisco, California.

II

The amount of the deficiency determined by the Commissioner against petitioner is $1,035.53 and is for income taxes [2] for the calendar year ended December 31, 1940. The amount thereof in controversy, as nearly as may be computed, is $909.82. The collection district in which the return for the period here involved is filed is the First District of California.

III

The notice of deficiency, a copy of which is attached hereto and marked "Exhibit A" was mailed to petitioner on May 26, 1942.

IV

The determination of tax set forth in said notice of deficiency is based upon the following errors:

1. The Commissioner in computing the gain realized from the sale of 212 shares of common stock of The Dow Chemical Company, a Michigan Corporation (hereinafter for convenience called "Dow"), assigned to each said shares a basis derived by dividing (i) the aggregate cost to petitioner of the entire block of 865 shares of preferred stock, $20 par value, and 250 shares of common stock, without par value, of Great Western Electro-Chemical Company, a California corporation (hereinafter for convenience called "Great Western"), held by petitioner immediately prior to the statutory merger of Great Western with and into Dow by

(ii) 412-3/16, being the number of the entire block of shares of common stock of Dow (of which said 212 shares were a part) acquired by petitioner on said [3] statutory merger.

2. The Commissioner in computing the gain realized from the sale of said 212 shares of common stock of Dow failed to assign as a basis of said 212 shares the basis to petitioner of the identical preferred and common shares of Great Western which on said statutory merger had been constituted, and converted into, said 212 common shares of Dow.

3. The Commissioner in computing the gain realized on the sale of said 212 common shares of Dow failed to identify said shares with, and trace them to, the identical preferred and common shares of Great Western which on said statutory merger had been converted into said 212 shares of Dow.

V

The facts upon which petitioner relies as sustaining the assignments of error are as follows:

1. Petitioner, on September 29, 1923, acquired 100 shares of preferred stock, $100 par value, of Great Western at a cost of $6,500.

2. Petitioner, on January 1, 1926, acquired 13 shares of preferred stock, $100 par value, of Great Western at a cost of $845.

3. Petitioner, on March 29, 1929, acquired 46 shares of preferred stock, $100 par value, of Great Western at a cost of $3,680. [4]

4. Petitioner, on March 30, 1929, acquired 46

shares of the common stock, $100 par value, of Great Western at a cost of $2,300.

5. In 1935 petitioner exchanged the 159 shares of preferred stock, $100 par value, of Great Western, acquired as set forth in paragraphs 1, 2 and 3 above, for 795 shares of the preferred stock, $20 par value, of Great Western, represented by certificates numbered P-392-398, inclusive, for 100 shares each and certificate numbered PL-145 for 95 shares.

6. Petitioner, in 1935, exchanged the 46 shares of common stock, $100 par value, of Great Western, acquired as set forth in paragraph 4 above, for 230 shares of common stock, without par value, of Great Western, represented by certificate numbers 273-274 for 100 shares each, and certificate numbered L-261 for 30 shares.

7. Petitioner, on April 14, 1936, acquired, at a cost of $1,583.75, 70 shares of preferred stock, $20 par value, of Great Western, represented by certificate numbered PL-414, and, on March 25, 1938, acquired, at a cost of $1,006, 20 shares, of the common stock, without par value, of Great Western, represented by Certificate numbered L-1178.

8. Petitioner immediately prior to the statutory merger of Great Western with and into Dow held said certificates numbered P-392-8, inclusive, for 100 shares each, certificate numbered PL 145 for 95 shares, and certificate numbered PL 414 for 70 shares, of the preferred stock, $20 par value, of [5] Great Western, and certificates numbered 273-274 for 100 shares each, and certificate numbered

L-261 for 30 shares, and certificate numbered L-1178 for 20 shares, of the common stock, without par value, of Great Western.

9. On or before December 31, 1938, Great Western merged with and into Dow under the terms and conditions of an agreement of statutory merger dated the 19th day of November, 1938, and pursuant to the applicable provisions of the laws of the State of California and the State of Michigan, being the respective states pursuant to and under the laws of which Great Western and Dow were incorporated.

10. Article III of said agreement of statutory merger provided that on the effective date thereof each issued share of the preferred stock, $20 par value, of Great Western (excepting such shares as were held by either Great Western or Dow) should constitute and be converted into 3/16ths of one full-paid and nonassessable common share of Dow and each issued share of common stock, without par value, of Great Western (excepting such shares as were held by either Great Western or Dow) should constitute and be converted into one full-paid and nonassessable common share of Dow.

11. Under and by virtue of the aforesaid provisions of Article III of said agreement of statutory merger, on and after the effective date thereof, the aforesaid certificates numbered P 392 to P 398, inclusive, each represented 18-3/4 [6] shares, said certificate numbered P L 145 represented 17-13/16 shares, said certificate numbered P L 414 represented 13-2/16 shares, said certificates numbered 273 and 274 each represented 100 shares, said certificate

numbered L 261 represented 30 shares, and said certificate numbered L 1178 represented 20 shares, of the common stock of Dow.

12. On January 30, 1939, petitioner exchanged said certificates hereinabove referred to for new certificates issued by Dow, as follows:

Certificates originally issued by Great Western	Dow common shares represented thereby on and after merger	New Dow Certificates	Dow common shares represented thereby
P 392-8	131-4/16)	(C 5822	100
PL 145	17-13/16)	(CO 18244	62
PL 414	13-2/16)	(CLF 171	3/16
273-4	200	C 5823-4	200 (100 shares each)
L 261	30)	CO 18245	50
L 1178	20)		

13. On March 4-5, 1940, petitioner sold 212 shares of the common stock of Dow for a total selling price of $33,264.24, 100 of which said 212 shares were represented by said certificate issued by Dow numbered C 5822 and 62 of which said 212 shares were represented by certificate issued by Dow numbered CO 18244 and 50 of which said 212 shares were represented by certificate issued by Dow numbered CO 18245. [7]

Wherefore, the petitioner prays that this Board may hear the proceeding and determine that the deficiency due from the petitioner for said calendar

year ended December 31, 1938, is not in excess of $125.71.

W. H. ORRICK
CHAS. L. BARNARD
Counsel for Petitioner.
W. H. Orrick
Chas. L. Barnard
405 Montgomery Street,
San Francisco, Calif.

Of Counsel:
Orrick, Dahlquist, Neff & Herrington,
405 Montgomery Street
San Francisco, California. [8]

State of California,
City and County of San Francisco—ss.

Amelia Davis Bloch, being duly sworn, says that she is the petitioner above named; that she has read the foregoing petition and is familiar with the statements contained therein, and that the facts stated are true.

AMELIA DAVIS BLOCH

Subscribed and sworn to before me this 17th day of August, 1942.

[Seal] HAZEL E. THOMPSON
Notary Public in and for the City and County of San Francisco, State of California.
My Commission Expires September 21, 1942. [9]

EXHIBIT A

Treasury Department
Internal Revenue Service
74 New Montgomery Street,
San Francisco, California
May 26 1942

Office of
Internal Revenue
Agent in Charge
San Francisco Division

IRA:90-D-WHL
(C:TS:PD
SF:WGW)

Mrs. Amelia Davis Bloch,
343 Sansome Street,
San Francisco, California.

Madam:

You are advised that the determination of your income tax liability for the taxable year ended December 31, 1940, discloses a deficiency of $1,035.53 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within 90 days (not counting Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are

requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, San Francisco, for the attention of Conference Section. The signing and filing of this form will expedite the closing of your return (s) by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

GUY T. HELVERING,
Commissioner,

By F. M. HARLESS
Internal Revenue Agent in Charge.

Enclosures:
Statement.
Form of waiver.

RR [10]

San Francisco
IRA:90-D-WHL
(C:TS:PD
SF:WGW)

Mrs. Amelia Davis Bloch,
343 Sansome Street,
San Francisco, California.

Tax Liability for the Taxable Year Ended December 31, 1940

	Liability	Assessed	Deficiency
Income tax	$34,254.17	$33,218.64	$ 1,035.53

In making this determination of your income tax liability, careful consideration has been given to your protest dated December 15, 1941, and to the statements made at the conferences held on January 9, 1942, and February 25, 1942.

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return		$86,932.29
Unallowable deductions and additional income:		
(a) Net long-term gain	$2,757.04	
(b) Salary income	200.00	
(c) Fiduciary income	157.50	3,114.54
Total		$90,046.83
Nontaxable income and additional deductions:		
(d) Interest on government obligations		157.55
Net income adjusted		$89,889.28

[11]

EXPLANATION OF ADJUSTMENTS

(a) You acquired 412 3/16 shares of common stock of The Dow Chemical Company in exchange for 865 shares of preferred stock and 250 shares of common stock of Great Western Electro-Chemical Company upon the consummation of a merger of the last-named corporation with The Dow Chemical Company. The merger was accomplished on or about December 31, 1938. That transaction was regarded as a reorganization upon which no gain or loss was recognizable for income tax purposes. In 1940 you sold 212 shares of common stock of The Dow Chemical Company, acquired through the above-mentioned reorganization, for $33,264.24 and claimed a cost basis of $13,900.17 and reported a capital gain attributable to these sales in the amount of $10,046.17. It is held that the cost basis of the stock sold is $8,185.32, and the capital gain attributable to these sales is $12,803.21, computed as follows:

Cost of preferred and common stock of Great Western Electro-Chemical Company surrendered in exchange for 412 3/16 shares of The Dow Chemical Company	$15,914.75
Cost of 1 share of The Dow Chemical Company	$ 38.61
Cost of 212 shares sold March 4, 5, 1940	$ 8,185.32
Selling price	33,264.24
Gain before capital gain adjustment	$25,078.92
Cost of stock held between 18 and 24 months	$ 1,006.00
Cost of stock held more then 24 months	14,908.75
Total	$15,914.75

1006
———— x $25,078.92 equals $1,582.48
15,914.75

Taxable at 66 2/3% ..... $ 1,054.99

14,908.75
———— x $25,078.92 equals $23,496.44
15,914.75

Taxable at 50% 11,748.22

Net taxable gain as revised	$12,803.21
Net taxable gain as reported	10,046.17
Increase	$ 2,757.04

[12]

(b) On your income tax return you claim a deduction of one-half of $400.00, namely $200.00, described as salary of secretary, and in your husband's return a similar amount is deducted. This was reported as an offset to your one-half share of your husband's income from salary from Crown Zellerbach Corporation and from fees as a director. The above-mentioned secretary is a regular employee of Crown Zellerbach Corporation. It is held that the amount claimed is not a deduction within the meaning of Section 23(a) of the Internal Revenue Code.

(c) The operating loss of $157.50 reported by

you as sustained by the trust of which you are a beneficiary is disallowed as not representing an allowable deduction within the meaning of section 23 (a) of the Internal Revenue Code.

(d) In your return you report interest on government obligations amounting to $4,069.39. Included in that amount is the sum of $3,938.75 reported as received by you as a beneficiary of a trust created by your husband. It has been determined that the taxable interest on government obligations received by you from the trust amounts to $3,781.20 and the amount reported reduced accordingly for the excess of $157.55.

COMPUTATION OF ALTERNATIVE TAX

Net income		$89,889.28
Minus:		
Net long-term capital gain		12,778.21
Ordinary net income		$77,111.07
Less:		
Personal exemption		none
Balance (surtax net income)		$77,111.07
Less:		
Interest on Government obligations, etc.	$3,911.84	
Earned income credit	1,400.00	5,311.84
Net income subject to normal tax		$71,799.23

[13]

Normal tax at 4 percent on $71,799.23	$ 2,871.97
Surtax on $77,111.07	24,435.54
Partial tax	$27,307.51
Plus:	
30 percent of net long-term gain	3,833.46
Alternative tax	$31,140.97

COMPUTATION OF TAX

Net income adjusted		$89,889.28
Less:		
Personal exemption		none
Balance (surtax net income)		$89,889.28
Less:		
Interest on government obligation	$3,911.84	
Earned income credit (10% of $14,000.00)	1,400.00	5,311.84
Net income subject to normal tax		$84,577.44
Normal tax at 4% on $84,577.44		$ 3,383.10
Surtax on $89,889.28		31,121.32
Total tax (ordinary)		$34,504.42
Total tax (Alternative tax in case of a net long term gain)		$31,140.97
Defense tax—10%		3,114.10
Total		$34,255.07
Less: Income tax paid at the source		.90
Correct income tax liability		$34,254.17
Income tax assessed:		
Original account No. 201815—First California		33,218.64
Deficiency of income tax		$ 1,035.53

[Endorsed]: U.S.B.T.A. Filed Aug. 21, 1942. [14]

[Title of Board and Cause.]

ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner admits and denies as follows:

I. Admits the allegations contained in paragraph I of the petition.

II. Admits the allegations contained in paragraph II of the petition, except that it is denied that the amount in controversy is as alleged in said paragraph.

III. Admits the allegations contained in paragraph III of the petition.

IV—1 to 3, inclusive. Denies that the Commissioner erred as alleged in subparagraphs 1 to 3, inclusive, of paragraph III of the petition.

V—1 to 4, inclusive. Admits the allegations contained in subparagraphs 1 to 4, inclusive, of paragraph V of the petition.

V—5 and 6. Denies the allegations contained in subparagraphs 5 and 6 of paragraph V of the petition. [15]

V—7. Admits that petitioner, on April 14, 1936, acquired, at a cost of $1,583.75, 70 shares of preferred stock, $20 par value, of Great Western, and, on March 25, 1938, acquired, at a cost of $1,006, 20 shares of the common stock, without par value, of Great Western; denies the remaining allegations

contained in subparagraph 7 of paragraph V of the petition.

V—8. Admits that petitioner immediately prior to the statutory merger of Great Western with and into Dow owned 865 shares of preferred stock, $20 par value, of Great Western, and 250 shares of common stock, without par value, of Great Western; denies the remaining allegations contained in subparagraph 8 of paragraph V of the petition.

V—9. Admits that on or about December 31, 1938, Great Western merged with and into Dow; denies the remaining allegations contained in subparagraph 9 of paragraph V of the petition.

V—10 to 12, inclusive. Denies the allegations contained in subparagraphs 10 to 12, inclusive, of paragraph V of the petition.

V—13. Admits that on March 4 and 5, 1940, petitioner sold 212 shares of the common stock of Dow for a total selling price of $33,264.24; denies the remaining allegations contained in subparagraph 13 of paragraph V of the petition.

VI. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's

determination [16] be approved and the petitioner's appeal denied.

(signed) J. P. WENCHEL
H. R. H.
Chief Counsel,
Bureau of Internal Revenue.

Of Counsel:
Alva C. Baird,
Division Counsel;
T. M. Mather,
Harry R. Horrow,
Special Attorneys,
Bureau of Internal Revenue.

HRH:sob 9-9-42

[Endorsed]: U.S.B.T.A. Filed Sept. 16, 1942.
[17]

The Tax Court of The United States

[Title of Cause.]

Docket No. 112225

STIPULATION

It is hereby stipulated by and between the parties hereto, through their respective counsel, that the following facts shall be taken as true and received as evidence in this proceeding, subject to the right of either party to introduce additional evidence not contrary to the facts herein stipulated:—

I

Taxpayer, on September 29, 1923, acquired 100

shares of Preferred Stock, $100 par value, of Great Western Electro-Chemical Company, (hereinafter for convenience called "Great Western"), at a cost of $6,500. [18]

II

Taxpayer, on January 1, 1926, acquired 13 shares of Preferred Stock, $100 par value, of Great Western, at a cost of $845.

III

Taxpayer, on March 29, 1929, acquired 46 shares of Preferred Stock, $100 par value, of Great Western, at a cost of $3,680.

IV

Taxpayer, on March 30, 1929, acquired 46 shares of Common Stock, $100 par value, of Great Western, at a cost of $2,300.

V

In 1935 Taxpayer, on the "recapitalization" of Great Western, exchanged the 159 shares of Preferred Stock, $100 par value, of Great Western, acquired as set forth in paragraphs I, II and III above, for 795 shares of Preferred Stock, $20 par value, of Great Western, represented by Certificates numbered P392 - 398, inclusive, for 100 shares each, and Certificate PL145 for 95 shares. No gain or loss was recognized on said exchange under Section 112 of the Revenue Act of 1934. [19]

VI

In 1935 Taxpayer, on the "recapitalization" of Great Western, exchanged the 46 shares of Common

Stock, $100 par value, of Great Western, acquired as set forth in paragraph IV above, for 230 Common Shares without par value of Great Western, represented by Certificates numbered 273 - 274 for 100 shares each, and Certificate L261 for 30 shares. No gain or loss was recognized on said exchange under Section 112 of the Revenue Act of 1934.

VII.

Taxpayer, on April 14, 1936, acquired 70 Preferred Shares, $20 par value, of Great Western, represented by Certificate No. PL414, at a cost of $1,583.75. On March 25, 1938, Taxpayer acquired 20 Common Shares without par value, of Great Western, represented by Certificate No. L1178, at a cost of $1,006.

VIII

Taxpayer, immediately prior to the Statutory Merger of Great Western with and into The Dow Chemical Company, (hereinafter called "Dow"), held Certificates Numbered P392-398 inclusive, each representing 100 Preferred Shares, $20 par value, of Great Western; Certificate No. PL145 for 95 Preferred Shares, $20 par value, of Great Western, and [20] Certificate PL414 representing 70 Preferred Shares, $20 par value, of Great Western; and Certificates Numbered 273-274, each representing 100 Common Shares, no par value, of Great Western; and Certificates No. L261 and L-1178 representing respectively 30 and 50 common shares without par value of Great Western.

IX

On or before December 31, 1938, Great Western merged with and into Dow, under the terms and conditions of an Agreement of Statutory Merger dated November 19, 1938, and pursuant to the applicable provisions of laws of the State of California and the State of Michigan, being the respective states pursuant to and under the laws of which Great Western and Dow were incorporated. There is attached hereto as Exhibit "A" and made a part hereof a copy of said Agreement of Statutory Merger dated November 19, 1938. Immediately prior to the date of said merger, Great Western was engaged, at its plant at Pittsburg, California, in the manufacturing, producing and selling of caustic soda, bleach, chloride of lime, liquid chlorine, zinc chloride and associated products extracted from salt and soda concentrates by the electro-chemical process. At said time Dow Chemical Company manufactured, at its plants at Midland and Mt. Pleasant, Michigan, more than two [21] hundred chemical products, including heavy chemicals, industrial chemicals, industrial chemicals, intermediate chemicals, solvents, dies, pharmaceutical chemicals, aromatic chemicals, insecticides, metals and alloys. At that time, Dow had affiliated with it the following companies: Ethyl-Dow Chemical Co., Io-Dow Chemical Co., Midland Ammonia Co., Dowell, Inc., Cliff's-Dow Chemical Co. On and after merger, Dow operated the business and assets of Great Western.

X

Under date of January 24, 1939, Taxpayer forwarded to The Cleveland Trust Company the certificates described in paragraph VIII above, under a letter of transmittal in the form attached hereto and marked Exhibit "B"; a copy of said letter of January 11, 1939, referred to in said letter of transmittal is attached hereto as Exhibit "C" and hereby made a part hereof. The Cleveland Trust Company cancelled said certificates so forwarded by Taxpayer and issued to Taxpayer the following numbered certificates of Dow, respectively in lieu of the following numbered certificates of Great Western so forwarded by Taxpayer:

Dow Certificates Issued	Dow Common Shares Represented Thereby	Great Western Certificates Cancelled
C5822	100 shares)	(P392 - 398
C18244	62 shares)	(PL145
CLF171	3/16ths)	(PL414
C5823	100 shares	273
C5824	100 shares	274
CO18245	50 shares)	(L261
	)	(L1178

[22]

XI

In March, 1940, Taxpayer sold 212 Common Shares of Dow for a total selling price of $33,264.24, 100 of which said 212 shares were represented by said Dow Certificate C5822 and 62 of which said 212 shares were represented by Dow Certificate CO18244 and 50 of which said 212 shares were represented by Dow Certificate CO18245.

Dated: January 30, 1943.

W. H. ORRICK
CHARLES L. BARNARD
Counsel for Petitioner.
J. P. WENCHEL
Chief Counsel
Bureau of Internal Revenue.

[23]

EXHIBIT "A"

Agreement of Statutory Merger (hereinafter called "this Agreement"), dated as of the 19th day of November, 1938, by and between The Dow Chemical Company, a corporation of the State of Michigan (hereinafter called the "Resulting Corporation") and its directors or a majority thereof, parties of the first part, and Great Western Electro-Chemical Company, a corporation of the State of California (hereinafter called "Great Western") and its directors or a majority thereof, parties of the second part.

Whereas, the Resulting Corporation is a corporation duly organized and existing under the laws of the State of Michigan; and Great Western is a corporation duly organized and existing under the laws of the State of California; and said two corporations, (being together hereinafter sometimes called the "constituent corporations") are authorized by their respective Articles of Association and Articles of Incorporation to carry on substantially the same or similar kinds of business; and

Whereas, the principal office and the registered

Exhibit "A"—(Continued)

office in the State of Michigan of the Resulting Corporation is in the City of Midland, in the County of Midland; and the principal office and place of business in the State of California of Great Western is at No. 9 Main Street, in the City and County of San Francisco; and

Whereas, the original Articles of Association of the Resulting Corporation were filed in the office of the Secretary of State of the State of Michigan on May 22nd, 1897; and the original Articles of Incorporation of Great Western were filed in the office of the Secretary of State of the State of California on January 10th, 1916; and

Whereas, under its Articles of Association filed in the office of the Secretary of State of the State of Michigan on May 22nd, 1897, and Articles filed June 25, 1925, continuing the corporate existence for a term of thirty years from May 18, 1927, as subsequently amended, the Resulting corporation has an authorized capital stock consisting of: 60,000 shares of 5% cumulative Preferred Stock of the par value of $100 each, all of which shares have been duly issued and at the date hereof are outstanding; and 2,000,000 shares of Common Stock without par value, of which 945,000 shares have been duly issued and at the date hereof are outstanding; and [24]

Whereas, under its Articles of Incorporation filed in the office of the Secretary of State of the State of California on January 10th, 1916, as subsepuently amended, Great Western has an authorized capital stock consisting of: 125,000 shares of 6%

Exhibit "A"—(Continued)

cumulative Preferred Stock of the par value of $20 each, of which 94,550 shares have been duly issued and at the date hereof are outstanding; and 125,000 shares of Common Stock without par value, of which 69,260 shares have been duly issued and at the date hereof are outstanding; and

Whereas, the respective Boards of Directors of the constituent corporations deem it advisable for the purpose of greater efficiency and economy in management and in other respects for the general welfare and advantage of said constituent corporations and their respective stockholders that said constituent corporations effect a statutory merger pursuant to a Plan of Reorganization, and said constituent corporations, respectively, desire to effect a statutory merger pursuant to such Plan of Reorganization and pursuant to the applicable provisions of the laws of the State of Michigan and the State of California, as respectively amended and supplemented;

Now Therefore, in consideration of the premises and of the mutual agreements, provisions, covenants and grants herein contained, the parties hereto hereby adopt and agree upon a Plan of Reorganization by statutory merger of said constituent corporations, as follows:

The parties hereto hereby agree, in accordance with the applicable provisions of said laws of the State of Michigan and of the State of California, as respectively amended and supplemented, that the constituent corporations shall effect a statutory merger, and be merged into one of such constituent

Exhibit "A"—(Continued)

corporations, to-wit, The Dow Chemical Company, the Resulting Corporation, and that the Resulting Corporation shall merge into itself Great Western; and that the terms and conditions of the merger hereby agreed upon (hereinafter called the "merger") and the mode of carrying the same into effect are, and shall be, as hereinafter set forth, that is to say:

Article I.

Except as hereinafter otherwise specifically set forth, the corporate name of the Resulting Corporation, to-wit, The Dow Chemical Company, and its identity, existence, [25] purposes, powers, objects, franchises, rights and immunities shall continue uneffected and unimpaired by the merger and the corporate franchises, entity, existence and rights of the other corporation party hereto, to-wit: Great Western, shall be merged into the Resulting Corporation, and the Resulting Corporation shall be fully vested therewith. The existence of Great Western, except in so far as it may be continued by statute, shall cease as soon as this Agreement shall have been adopted or apporoved by the requisite votes of holders of the capital stock of each of said constituent corporations in accordance with the provisions of this agreement and in accordance with the applicable provisions of the laws of the respective states under which said constituent corporations were formed and upon the doing of such other acts or things as shall be required for accomplishing the Statutory Merger by the laws of the respective states under which said constituent

Exhibit "A"—(Continued)

corporations were formed; and thereupon said constituent corporations shall be merged into one of said constituent corporations, to-wit: said The Dow Chemical Company, the Resulting Corporation, one of the parties of the first part hereto; and

It is agreed that the meeting of stockholders of the respective constituent corporations for the adoption or rejection of this agreement shall be held on December 22, 1938, or on such later date as shall be mutually agreed upon by a majority of the Board of Directors of each constituent corporation and that forthwith upon the approval of this agreement by the stockholders of the constituent corporations, the officers and directors of the respective constituent corporations will take all necessary steps required by the applicable statutes to effectuate the merger. Said constituent corporations shall be deemed merged upon the doing by them and each of them and by their respective Boards of Directors, officers and shareholders of all the acts and things required by the laws of the States of California and Michigan for the effectuation of a statutory merger of a domestic and a foreign corporation, including the filing in the office of the Secretary of State of the State of Michigan of the documents specified in Section 52 of the Michigan General Corporation Act and the filing in the office of the Secretary of State of the State of California of the documents specified in Sections 361 and 361-a of The Civil Code of the State of California. The date upon which said constituent corporations

Exhibit "A"—(Continued)

shall be so merged is hereinafter referred to as "the effective date of this agreement."

Article II.

The laws of the State of Michigan are hereby selected as the laws which shall govern the Resulting Corporation. The Articles of Association and By-Laws of The Dow Chemical Company, [26] as amended prior to the date of this Agreement, and as may be further amended hereafter pursuant to law, shall be and continue to be the Articles of Association and By-Laws of the Resulting Corporation; and the directors and officers of The Dow Chemical Company on the effective date of this Agreement shall continue to be the directors and officers of the Resulting Corporation, until their successors shall be elected and qualified.

Article III.

The mode of carrying the Merger into effect and the manner and basis of causing the shares of stock, and all rights in respect thereof, of Great Western outstanding as of the effective date of this Agreement, to constitute or to be converted, forthwith upon the effective date of this Agreement, into shares of the Resulting Corporation, are as follows:

Subdivision A: Each issued share of 6% cumulative Preferred Stock, $20 par value, of Great Western, except shares held by a constituent corporation, shall constitute and be converted into three-sixteenths (3/16th) of one (1) full-paid and non-assessable share of Common Stock without par value of the Resulting Corporation.

Each issued share of Common Stock without

Exhibit "A"—(Continued)

par value of Great Western, except shares held by a constituent corporation, shall constitute and be converted into one (1) full-paid and non-assessable share of Common Stock without par value of the Resulting Corporation.

As soon as practicable after the effective date of this agreement the Resulting Corporation will deliver to holders of certificates, which represent shares of the Capital Stock of Great Western, in full satisfaction of all rights evidenced by such certificates (except those holders who shall not have approved of the Merger and who shall have demanded the fair market value of their shares as provided by law), certificates representing shares of its Common Stock without par value in exchange, on the basis hereinabove set forth, for and against the surrender for cancellation of certificates which represent shares of the capital stock of Great Western, duly endorsed in blank, if required, to the Resulting Corporation at such place as may be designated by the Resulting Corporation.

Upon approval of this Agreement by the stockholders of the Resulting Corporation and Great Western, the Resulting Corporation agrees forthwith to take appropriate steps to list upon the New York and Cleveland Stock Exchanges and register for listing thereon under the Securities Exchange Act of 1934 the additional shares of its stock which are required to be delivered to the shareholders of Great Western. [27]

No fractions of shares of Common Stock of the Resulting Corporation shall be issued upon the

Exhibit "A"—(Continued)

conversion of 6% cumulative Preferred Stock of Great Western into Common Stock of the Resulting Corporation on the basis hereinabove set forth, but the Resulting Corporation shall, in lieu of fractional shares, issue non-voting and non-dividend paying scrip certificates, running in favor of the bearer thereof, entitling each holder of such scrip certificates to receive (on surrender thereof within one (1) year after the effective date of this Agreement, together with other scrip certificates of like tenor, representing rights in respect to one or more full shares of Common Stock of the Resulting Corporation) a certificate for the number of shares of Common Stock of the Resulting Corporation, equal to the number of full shares of Common Stock of the Resulting Corporation, represented by such scrip certificates. All such scrip certificates which are not surrendered within the time aforesaid shall be void and of no effect whatsoever on and after a date which shall be one (1) year after the effective date of this Agreement, except that the holders thereof shall be entitled to receive upon surrender thereof their pro rata portion of the proceeds resulting from the sale (which may be effected publicly or privately at their currently prevailing prices) of the full shares of stock of the Resulting Corporation representing such unsurrendered scrip certificates; such sale to be made by the transfer agent of the shares with respect to which such scrip certificates were issued, as agent for and on behalf of the holders of such scrip certificates.

Exhibit "A"—(Continued)

If prior to the effective date of this Agreement the constituent corporations shall acquire in any manner any shares of stock of any class of Great Western, then on said date such shares shall be cancelled and all rights in respect thereof shall cease.

Subdivision B: The shares of 5% cumulative Preferred Stock, $100 par value, and Common Stock without par value of The Dow Chemical Company outstanding upon the effective date of this Agreement shall continue to be outstanding as shares of the Resulting Corporation and the certificates representing such shares shall not be surrendered nor shall the holders of said certificates receive any other shares or certificates by reason of this Agreement.

Article IV.

On the effective date of this Agreement, as provided in and by the applicable statutes, all and singular the rights, [28] privileges, powers and franchises, as well of a public as of a private nature, of Great Western, and all property, real, personal and mixed, of Great Western, and all debts due to Great Western on whatever account, and all other things in action or belonging to Great Western, shall be vested in the Resulting Corporation; and all property, rights, privileges, powers and franchises, and all and every other interest of Great Western, shall be thereafter as effectually the property of the Resulting Corporation as they were of Great Western, and the title to any real or personal property, whether by deed or other-

Exhibit "A"—(Continued)

wise, vested in Great Western, shall not revert or be in any way impaired by reason of the Merger; Provided that all rights of creditors and all liens upon the property of Great Western shall be preserved unimpaired and all debts, liabilities and duties of Great Western shall thenceforth attach to said Resulting Corporation and may be enforced against it to the same extent as if said debts, liabilities and duties had been incurred or contracted by it. And the parties of the second part hereto hereby agree that from time to time, as and when requested by the Resulting Corporation, or by its successors or assigns, they will execute and deliver or cause to be executed and delivered all such deeds and other instruments, and will take or cause to be taken such further or other action, as the Resulting Corporation may deem necessary or desirable, in order to vest in and confirm to the Resulting Corporation title to and possession of all said property, rights, privileges, powers and franchises and otherwise to carry out the intent and purpose of this Agreement.

Article V.

The Resulting Corporation shall pay all expenses of carrying this Agreement into effect and of accomplishing the Merger.

Article VI.

The Resulting Corporation agrees that, from and after the effective date of this Agreement, it may be served with process in the State of California in any proceeding for enforcement of any obliga-

Exhibit "A"—(Continued)

tion of Great Western; and the Resulting Corporation will upon the effective date of this Agreement designate some person residing within the State of California upon whom process directed to the Resulting Corporation in such a proceeding may be served, and the complete business or residence address of such person, and give its irrevocable consent to such service and the Resulting Corporation hereby agrees that, in the absence of such designation, service of such process on the Secretary of State of the State of California shall be [29] deemed to be due service upon the Resulting Corporation.

Article VII.

This Agreement shall be submitted to the stockholders of each of the constituent corporations as provided by law and it shall take effect and be deemed and taken to be the Agreement and act of Merger of said corporations upon the adoption thereof by the votes, given in person or by proxy, of holders of shares of the capital stock of each of said constituent corporations in accordance with the requirements of the laws of the state under the laws of which each was formed at a meeting of the stockholders of each of said constituent corporations held for the purpose of considering and voting for the adoption or rejection of this Agreement, and upon the doing of such other acts and things as shall be required for accomplishing the Merger by the applicable provisions of said laws of the State of Michigan and of the State of California, as respectively amended and supplemented.

Exhibit "A"—(Continued)

wise, vested in Great Western, shall not revert or be in any way impaired by reason of the Merger; Provided that all rights of creditors and all liens upon the property of Great Western shall be preserved unimpaired and all debts, liabilities and duties of Great Western shall thenceforth attach to said Resulting Corporation and may be enforced against it to the same extent as if said debts, liabilities and duties had been incurred or contracted by it. And the parties of the second part hereto hereby agree that from time to time, as and when requested by the Resulting Corporation, or by its successors or assigns, they will execute and deliver or cause to be executed and delivered all such deeds and other instruments, and will take or cause to be taken such further or other action, as the Resulting Corporation may deem necessary or desirable, in order to vest in and confirm to the Resulting Corporation title to and possession of all said property, rights, privileges, powers and franchises and otherwise to carry out the intent and purpose of this Agreement.

Article V.

The Resulting Corporation shall pay all expenses of carrying this Agreement into effect and of accomplishing the Merger.

Article VI.

The Resulting Corporation agrees that, from and after the effective date of this Agreement, it may be served with process in the State of California in any proceeding for enforcement of any obliga-

Exhibit "A"—(Continued)

tion of Great Western; and the Resulting Corporation will upon the effective date of this Agreement designate some person residing within the State of California upon whom process directed to the Resulting Corporation in such a proceeding may be served, and the complete business or residence address of such person, and give its irrevocable consent to such service and the Resulting Corporation hereby agrees that, in the absence of such designation, service of such process on the Secretary of State of the State of California shall be [29] deemed to be due service upon the Resulting Corporation.

Article VII.

This Agreement shall be submitted to the stockholders of each of the constituent corporations as provided by law and it shall take effect and be deemed and taken to be the Agreement and act of Merger of said corporations upon the adoption thereof by the votes, given in person or by proxy, of holders of shares of the capital stock of each of said constituent corporations in accordance with the requirements of the laws of the state under the laws of which each was formed at a meeting of the stockholders of each of said constituent corporations held for the purpose of considering and voting for the adoption or rejection of this Agreement, and upon the doing of such other acts and things as shall be required for accomplishing the Merger by the applicable provisions of said laws of the State of Michigan and of the State of California, as respectively amended and supplemented.

Exhibit "A"—(Continued)

Article VIII.

It is agreed that the Resulting Corporation shall not, after the date hereof and prior to the effective date of this Agreement, declare or pay any dividend or make any distribution to holders of its Common Stock, except dividends heretofore declared, and the Great Western shall not, after the date hereof and prior to the effective date of this Agreement, declare or pay any dividend or make any distribution to holders of its Preferred or Common Stock, except dividends heretofore declared.

In Witness Whereof, the constituent corporations have caused this Agreement to be signed in their respective corporate names by their respective Presidents or one of their respective Vice-Presidents and their respective Secretaries or one of their respective Assistant Secretaries, and their respective corporate seals to be hereunto affixed and attested, and a majority of the directors of each of said corporations have duly subscribed their names to this Agreement, all as of the day and year first above written.

[Seal] THE DOW CHEMICAL COMPANY

By WILLARD H. DOW,
President.

And by EARL W. BENNETT,
Secretary.

Exhibit "A"—(Continued)

E. O. BARSTOW
EARL W. BENNETT
J. S. CRIDER
WILLARD H. DOW
JAMES T. PARDEE
C. J. STROSACKER
W. R. VEAZEY
LELAND I. DOAN

Being a majority of the Directors of The Dow Chemical Company. [30]

[Seal] GREAT WESTERN ELECTRO-CHEMICAL COMPANY

By J. F. C. HAGENS,
President.

And by M. FLEISHHACKER, JR.,
Secretary.

LOUIS BLOCH
M. FLEISHHACKER
M. FLEISHHACKER, JR.
MARK L. GERSTLE
J. F. C. HAGENS
CHAFFEE E. HALL
C. W. SCHEDLER
J. F. SHUMAN
JOHN G. SUTTON

Being a majority of the Directors of Great Western Electro-Chemical Company.

(Certifications, County Clerk's Certificates and Certifications omitted.) [31]

EXHIBIT "B"

Letter of Transmittal
To Accompany Certificates for Shares of Capital Stock of Great Western Electro-Chemical Company

Before Executing Please Read Carefully
the Instructions on the Reverse Hereof

....., 1939

The Cleveland Trust Company, Agent
916 Euclid Avenue
Cleveland, Ohio

Gentlemen:

Receipt of the printed letter dated January 11, 1939 from the President of The Dow Chemical Company to the shareholders of Great Western Electro-Chemical Company is acknowledged. The undersigned encloses herewith for surrender the following certificate(s) for shares of Capital Stock of Great Western Electro-Chemical Company:

Certificate No.	No. of Shares	Name in Which Registered
Preferred	.....	.....
.....	.....	.....
Common	.....	.....
.....	.....	.....

It is understood that at the earliest practicable time after receipt of the above listed stock certificate (s) you will deliver, as indicated below, certificate(s) representing whole shares of common stock without par value of The Dow Chemical Company, (a) in the ratio of 3/16ths of a share of such stock for each share of 6% cumulative preferred stock, $20 par value, of Great Western

Electro-Chemical Company represented by the enclosed stock certificate(s) [together with non-voting and non-dividend paying scrip certificate(s) for the fractional share, if any, of such stock to which the undersigned would otherwise be entitled], and (b) in the ratio of one share of such stock for each share of common stock without par value of Great Western Electro-Chemical Company represented by the enclosed stock certificate(s).

Kindly issue stock certificate(s), and scrip certificate(s), if any, as follows:

Name.....
(Print name in full)
Address.....
(Street and Number)
.....
(City) (State) [32]

and deliver same as follows:

check one [ ] against window receipt
or
[ ] by registered mail to:

(Fill in only if you desire certificate to be mailed)

Please Leave Blank
Receipt Issued .....
Approved .....
Certificates Issued
.....
.....
.....
Date Delivered .....

Name .....
(Print Name in Full)
Address .....
(Street and Number)
.....
(City) (State)
Signature .....
(Presentor Signs)

(Reverse side of Letter of Transmittal)

Instructions

1. The certificates must be duly endorsed in blank for transfer or accompanied by proper in-

struments of transfer in blank. The signature must correspond with the name as written upon the face of the certificate in every particular, without alteration or enlargement or any change whatever, and the signature must be properly guaranteed by a Cleveland or New York City bank or trust company, or a bank or trust company having a Cleveland or New York City correspondent, or a brokerage firm having membership in the New York Stock Exchange or the Cleveland Stock Exchange.

2. If the certificates for shares of common stock without par value of The Dow Chemical Company are to be issued in a name other than the name set forth in the surrendered certificates, this letter of transmittal must be accompanied by appropriate Federal transfer tax stamps or funds sufficient to purchase the same in the amount of: 5c for each $100 of par value, or fraction thereof, of the preferred shares, $20 par value each; and 5c for each share of common stock without par value surrendered if sale price is $20 or more per share. Note: if sale price is less than $20 per share (either class) or if transfer does not constitute a sale, the above tax rate shall be 4c instead of 5c.

3. If your shares are pledged as collateral for a loan with a bank or a broker, it is suggested that you arrange with such bank or broker to forward the certificates therefor.

4. Certificates presented by executors, administrators, trustees and other fiduciaries must be accompanied by proper evidence of authority.

5. Certificates should be forwarded by registered mail to The Cleveland Trust Company, Corporate Trust Department, 916 Euclid Avenue, Cleveland, Ohio. [33]

EXHIBIT "C"

The Dow Chemical Company
Midland, Michigan, U. S. A.
January 11, 1939

To the Shareholders of
Great Western Electro-Chemical Company:

You are hereby notified that the agreement of statutory merger between The Dow Chemical Company and Great Western Electro-Chemical Company has become effective and, pursuant to its provisions, the holders of shares of 6% cumulative preferred stock, (illegible) par value each, of Great Western Electro-Chemical Company are entitled to receive 3/16ths of a share of common stock without par value of the Dow Chemical Company for each shares of said preferred stock so held by them respectively, and the holders of common stock without par value of Great Western Electro-Chemical Company are entitled to receive one share of common stock without par value of the Dow Chemical Company for each share of common stock of Great Western Electro-Chemical Company so held by them respectively, upon the surrender for cancellation of certificates representing shares of Great Western Electro-Chemical Company duly endorsed in blank.

The Cleveland Trust Company, Cleveland, Ohio, has been authorized and instructed to issue certifi-

cates for shares of the common stock of the Dow Chemical Company in exchange for stock certificates of Great Western Electro-Chemical Company in manner above provided upon surrender of such certificates. Script certificates will be issued in lieu of fractional shares and the Company will endeavor to arrange for the sale or purchase of scrip certificates to accommodate their holders. You will be fully advised of any such arrangement when scrip certificates are issued. An addressed envelope and form of letter of transmittal are enclosed for your convenience in mailing stock certificates for exchange. Please read carefully the instructions on reverse side of letter of transmittal and make certain that signatures are guaranteed in the manner indicated by these instructions.

The Board of Directors of the Dow Chemical Company intends to declare a dividend on common stock payable on Frebruary 15 to stockholders of record at the close of business on February 1, 1939, and to avoid confusion and unnecessary accounting desires that the exchange of certificates be completed at the earliest practicable date. Your cooperation will be appreciated.

Very truly yours,
THE DOW CHEMICAL
COMPANY
WILLARD H. DOW,
President

[Endorsed]: T. C. U. S., Filed Feb. 1, 1943. [34]

OFFICIAL REPORT OF PROCEEDINGS
BEFORE THE
U. S. BOARD OF TAX APPEALS

Docket No. 112224
Docket No. 112225

In the Matter of

LOUIS BLOCH and
AMELIA DAVIS BLOCH,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Hearing at San Francisco California

Date February 1, 1943 [35]

[Title of Tax Court and Cause.]

REPORTER'S MINUTES

Hearing at Federal Court Room No. 401,
Civic Auditorium, San Francisco, California,
on the 1st day of February, 1943, at
11-10 o'clock A. M.

The above-entitled proceeding came on for hearing on this 1st day of February, 1943, before the Honorable Charles P. Smith, Judge, The Tax Court of the United States at San Francisco, California

pursuant to notice of hearing heretofore given, whereupon the following proceedings were had, to-wit:

Appearances:

CHARLES L. BARNARD (405 Montgomery Street San Francisco, California)
Appearing on behalf of Petitioners.

HARRY R. HORROW, (Honorable J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue), appearing on behalf of Commissioner of Internal Revenue, Respondent. [36]

PROCEEDINGS

Judge Smith: Docket No. 112224, Louis Bloch and Docket No. 11225, Amelia Davis Bloch, I believe it was said that there was no evidence to offer. Is that correct?

Mr. Barnard: That is correct. The government and petitioners have entered into a stipulation of facts, your Honor, but there is one additional point to be covered by a stipuation made of record.

At the time the petition was filed there were certain deductions that were disallowed on the Higgins case. Since the petition was filed the Higgins case has been, in effect, overruled by the 1942 Act provision and in order to save our rights a stipulation is to be read into the record that this deduction shall be allowed in part. Mr. Horrow has the computation on that.

Mr. Horrow: If your Honor please, we are prepared to stipulate that the taxpayer in the case of

Louis Bloch paid during the taxable year $200 as secretarial expense and $60 for expense in connection with a safe deposit box and that the portion of said total amount of $260 which is allowable as a deduction under Section 121 of the Revenue Act of 1942 is the proportion which the tax exempt interest received by the Taxpayer during the year 1940 in the amount of $11,781.88 bears to the total amount of income, taxable and non-taxable, received by the taxpayer during the taxable year. The total [37] taxable income received consists of dividends in the amount of $67,408.77, interest in the amount of $445.54 and gross capital gains in the amount of $29,937.01. The latter amount is still in issue, your Honor, so we cannot stipulate as to the exact amount allowable under the Revenue Act of 1942 for the reason that the amount of capital gains is subject to a determination by your Honor on the basis of the stipulation of facts to be filed.

The figures with respect to Amelia Davis Bloch are as follows:

Taxpayer paid the same amount, $200 for secretarial expense, and that we stipulate that a portion of that is allowable as a deduction under Section 121 of the Revenue Act of 1942 to be based on the proportion which the tax exempt interest received by the taxpayer during the taxable year in the amount of $11,867.32 bears to the total income received during that year, both taxable and non-taxable; the taxable income being interest in the amount of $3,956.84, dividends in the amount of $47,062.02, and capital gains in the amount of

$25,078.92. The latter amount is still in dispute because an issue remains as to the amount of capital gains realized by the taxpayer during the year.

Mr. Barnard: There is an ambiguity in the statement of counsel for the government, but I think we both mean the same thing: that there will be disallowed of the amounts paid [38] only such portion as the exempt interest bears to the total income.

Is that correct, Mr. Horrow?

Mr. Horrow: That is correct, your Honor, the total income as finally determined in these matters.

Mr. Barnard: Your Honor, the main question here involves the point as to whether the rule of the Fleischmann case on the identification is applicable to a statutory merger. As far as petitioner is concerned we *would must* as well let the matter be submitted on brief and the stipulation of facts, if that is satisfactory to counsel for the government.

Mr. Horrow: That is satisfactory, your Honor.

Judge Smith: You mean a further stipulation of facts?

Mr. Barnard: No. There is a stipulation of facts that will be submitted herein.

Judge Smith: And counsel desire to file briefs in the case?

Mr. Barnard: Yes. 45, 30, and 15.

Mr. Horrow: I should like to file a stipulation of facts in these cases, your Honor.

Mr. Barnard: Yes.

Mr. Horrow: I now file the stipulation in the case [39] of Louis Bloch and ask that it be received.

Judge Smith: The stipulation of facts will be received.

Mr. Horrow: I also file the stipulation of facts in the case of Amelia Davis Bloch.

Judge Smith: That stipulation of facts is also received.

Mr. Horrow: Has your Honor set the date for briefs?

Judge Smith: Yes. Counsel for the petitioners may have until March 20th. State for the record the name of the petitioners' counsel.

Mr. Barnard: Charles L. Barnard.

Judge Smith: Have you filed an appearance slip in the case?

Mr. Barnard: Yes. I am appearing of record.

Judge Smith: Counsel for the petitioners then may have until March 20th for the filing of a brief.

Mr. Barnard: Thank you.

Judge Smith: The respondent may have until April 20th for the filing of a brief and then the petitioners' counsel may have until May 5th for the filing of a reply, if he desires to file any reply.

Mr. Horrow: Thank you, your Honor.

(Hearing concluded)

[Endorsed]: T. C. U. S. Filed Feb. 24, 1943.

[40]

The Tax Court of the United States

[Title of Causes.]

Docket Nos. 112224, 112225

W. H. ORRICK, Esq., and
CHARLES L. BARNARD, Esq.,
for the petitioners.

HARRY R. HORROW, Esq.,
for the respondent.

MEMORANDUM OPINION

Smith, Judge: These proceedings, consolidated for hearing, are for the redetermination of income tax deficiencies for the calendar year 1940 in the amounts of $451.13 and $1,035.53, respectively. The issue presented is whether the respondent erred in determining the basis of certain shares of stock of the Dow Chemical Co. sold by the petitioners during the taxable year by averaging the cost of shares of Great Western Electro-Chemical Co. which were exchanged by petitioners therefor in a nontaxable reorganization. [41]

The parties have stipulated that the petitioners are entitled to additional deductions under section 121 of the Revenue Act of 1942, the final amounts to be computed after a determination of the taxable income resulting from the transactions here in question.

All of the facts have been stipulated.

The petitioners are residents of California and filed their income tax returns for 1940 with the

collector of internal revenue for the first district of California.

In 1940 the petitioner Louis Bloch sold 215 common shares of Dow Chemical Co., hereinafter called Dow, for a total selling price of $33,525.02 and petitioner Amelia Davis Bloch sold 212 like shares for a total selling price of $33,264.24. These certificates were received by the petitioners in 1939 under a statutory merger of Great Western Electro-Chemical Co., hereinafter called Great Western, a California corporation, and Dow, a Michigan corporation. The shares of Dow sold by the petitioners in 1940 are traceable through stock certificate numbers to specific shares of Great Western which were turned in in exchange. The cost to petitioner Louis Block of the Great Western shares later represented by the Dow shares sold was $5,685.86 and the cost of the 212 shares of such stock sold by petitioner Amelia Davis Bloch was $13,900.17. They used such cost bases in determining the capital gains attributable to the sales made by them.

In his determination of the deficiencies the respondent has held that the petitioners may not use such cost bases but must use in lieu thereof the cost of each Dow share determined by dividing the total cost of the Great Western shares acquired by each at different times and different [42] prices by the total number of Dow shares received and then multiplying that amount by the number of Dow shares sold by each.

The only question presented for decision relates to the basis. No contention is made that the peti-

tioners' bases used are not correct provided they may trace the Dow shares sold by specific certificate numbers to the Great Western shares purchased.

There is no question but that the Dow shares were received by the petitioners in 1939 upon a reorganization under section 112 (g) (1) I.R.C. Neither is there any question but that the following portion of section 113 I.R.C. is applicable in the determination of the basis of the shares:

> Sec. 113. Adjusted Basis for Determining Gain or Loss.
>
> (a) Basis (Unadjusted) of Property.—The basis of property shall be the cost of such property; except that——
>
> * * * * * *
>
> (6) Tax-free exchanges generally.—If the property was acquired, after February 28, 1913, upon an exchange described in section 112 (b) to (e), inclusive, the basis (except as provided in paragraphs (15), (17), or (18) of this subsection) shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the taxpayer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. * * *

The respondent contends that no identification of the shares of Dow stock received in exchange for Great Western shares is permissible and that the basis of the Dow shares should be computed by di-

viding the total cost of the Great Western shares by the total number of Dow shares received. In support of such proposition the respondent cites Commissioner v. Oliver (C.A.A., 3rd Cir.), 78 Fed. (2d) 561; Helvering v. Stifel (C.C.A., 4th Cir.), [43] 75 Fed. (2d) 583; Commissioner v. Von Gunten (C.C.A., 6th Cir.), 76 Fed. (2d) 670, and Commissioner v. Bolender (C.C.A., 7th Cir.), 82 Fed. (2d) 591. Respondent submits that in those cases:

> * * * the courts rejected the "first in first out" rule which the Commissioner had contended was applicable in the absence of identification. But under the rationale of those cases it is clear that attempts to establish the cost basis of the shares received by identification would be equally futile. Identification is permissible only when there is identity between the shares of stock sought to be identified. * * *
>
> In Raoul H. Fleischmann, 40 B.T.A. 672, 688, we said:
>
> * * * It is now well established that where stock of one corporation is exchanged for stock of another, in pursuance of a plan of reorganization, the basis of the shares surrendered (after adjustment for any recognized gain or loss) must be allocated equally to the shares acquired, and the cost of some particular lot of the old shares may not be allocated to some particular lot of the new shares. * * *

Under the rule identification of the shares of a recognized corporation with those of another corporation is immaterial. As said by the Circuit Court

of Appeals for the Third Circuit in Arrott v. Commissioner .....Fed. (2d).....(June 9, 1943):

> We think it is the only sound rule. The old shares all have the same exchange value for the new ones no matter what they cost the taxpayer. He gets as much new stock for the share for which he paid $80 as he does for the share for which he paid $120. The old shares lose their identity when traded for the new, just as the money with which one buys a war bond loses its identity in the certificate, though to the purchaser some of it may have been a gift, some won on a horse race and the remainder earned by the sweat of his brow. The old shares are gone; the new shares in what is at least nominally a new company take their place. Each new share costs the taxpayer the quotient of the sum of the cost of the old shares divided by the number of new shares he receives.

The respondent's determination of basis is approved.

Decisions will be entered under Rule 50.

Entered: Aug. 1, 1943. [44]

The Tax Court of the United States
Washington

Docket No. 112225

AMELIA DAVIS BLOCH,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

The computation of the respondent filed with the Court on September 2, 1943 has been examined and found to be in accordance with the determination of the Court as set forth in its report. Petitioner therefore joins with the respondent in praying that the Court enter its decision based upon such computation, reserving however the right to contest the correctness of such decision in the appellate courts as provided by statute.

W. H. ORRICK
CHAS. L. BARNARD
(Signature)
405 Montgomery Street
(Office Address)
San Francisco, 4, California
Attorneys for Petitioner.

[Endorsed]: T. C. U. S. Filed Oct. 2, 1943. [45]

The Tax Court of the United States
Washington

Docket No. 112225

AMELIA DAVIS BLOCH,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the Memorandum Opinion entered August 14, 1943, the respondent herein having on September 2, 1943, filed a recomputation of tax and the petitioner having on October 2, 1943, filed an acquiescence therein, now therefore, it is

Ordered and Decided: That there is a deficiency in income tax for the calendar year 1940 in the amount of $932.75.

(Signed) CHARLES P. SMITH
Judge.

[Entered]: Oct. 5, 1943. [46]

[Title of Tax Court and Cause.]

PETITION FOR REVIEW

Amelia Davis Bloch, taxpayer, the petitioner in this cause, by W. H. Orrick and Charles L. Barnard, counsel, hereby files her petition for a review by the United States Circuit Court of Appeals for the

Ninth Circuit of the decision of The Tax Court of the United States rendered on October 5, 1943 determining a deficiency in the petitioner's Federal income tax for the calendar year 1940 in the amount of $932.75, and respectfully shows:

I.

Venue

The petitioner is an individual whose mailing address is 343 Sansome Street, San Francisco, California [47] and whose residence address is 20 Cherry Street, San Francisco, California. The income tax return of the petitioner for the calendar year 1940 was made and filed with the Collector of the First District of California whose office is and at all times herein mentioned was located at San Francisco, California.

II.

Nature of Controversy

The controversy involves the proper determination of petitioner's liability for Federal income taxes for the calendar year 1940, and, specifically, the proper basis to be used in determining the gain realized by petitioner from the sale by her in March, 1940, for a total selling price of $33,264.24, of 212 common shares of The Dow Chemical Company, without par value, represented by Certificates Nos. C5822, CO18244 and CO18245, respectively for 100, 62 and 50 shares.

The circumstances under which petitioner acquired the shares so sold are as follows:

Petitioner, immediately prior to the statutory merger of Great Western-Electro Chemical Company with and into The Dow Chemical Company, hereinafter referred to, held the following numbered stock certificates of Great Western Electro-Chemical Company, representing respectively the [48] shares of said company below indicated, viz:

Certificate No.	Shares Represented
P392 - P398, inclusive	100 - $20 par value Preferred Shares each.
PL-145	95 - $20 par value Preferred Shares.
PL-414	70 - $20 par value Preferred Shares.
273 - 274, inclusive	100 - no par value Common Shares each.
L-261	30 - no par value Common Shares.
L-1178	50 - no par value Common Shares.

On or before December 31, 1938 Great Western Electro-Chemical Company merged with and into The Dow Chemical Company, under the terms and conditions of an Agreement of Statutory Merger dated November 19, 1938 and pursuant to the applicable provisions of the laws of the State of California and the State of Michigan, being the states under the laws of which Great Western Electro-Chemical Company and The Dow Chemical Company respectively were incorporated. Under and by virtue of said Agreement of Statutory Merger, on the effective date thereof, the outstanding and issued shares of Great Western Electro-Chemical Company (excepting only shares held by The Dow Chemical Company or Great Western Electro-Chemical Company) were constituted and converted into full paid and non-assessable common shares,

without par value, of The Dow Chemical Company as follows, viz: [49]

Great Western Electro-Chemical Company Shares	The Dow Chemical Company Shares
1 Preferred Share—$20 par value	3/16 Common Share, without par value
1 Common Share—without par value	1 Common Share, without par value

On or about January 31, 1939 said above mentioned certificates were cancelled and there was issued to petitioner the following numbered certificates of The Dow Chemical Company respectively in lieu of the following numbered certificates of Great Western Electro-Chemical Company so cancelled:

Dow Certificates Issued	Dow Common Shares Represented Thereby	Great Western Certificates Cancelled
C5822	100 shares)	(P392-398
C18244	62 shares)	(PL145
CLF171	3/16ths)	(PL414
C5823	100 shares	273
C5824	100 shares	274
CO18245	50 shares)	(L261
	)	(L1178

Petitioner, in her income tax return for the calendar year 1940, determined the gain on said sale of said 212 common shares of The Dow Chemical Company, without par value, by assigning to the said shares the same basis as the basis of the identical shares of Great Western Electro-Chemical Company from which they were converted. The respondent held that for the purpose of determining said gain the basis of said 212 shares was the average of all shares of Great Western Electro-Chemical

Company held by petitioner on the effective date of [50] said statutory merger and, on the basis thereof and matters not here in controversy, determined a deficiency for the calendar year 1940 against taxpayer in the amount of $1,035.53. Petitioner filed her petition with The Tax Court of the United States (then "United States Board of Tax Appeals") for a redetermination of said deficiency and said Court sustained the holding of the Commissioner and determined the aforementioned deficiency in the amount of $932.75 against petitioner. The difference in the amount of the deficiency determined by the respondent (viz: $1,035.53) and the amount of the deficiency determined by The Tax Court of the United States (viz: $932.75) arises from the decision of The Tax Court of the United States in respect of said matters not here in controversy, which said decision as to said other matters is based on a stipulation between the parties.

W. H. ORRICK
CHARLES L. BARNARD
Counsel for Petitioner.

W. H. ORRICK
CHARLES L. BARNARD
405 Montgomery Street
San Francisco, 4, Calif. [51]

State of California
City and County of San Francisco—ss.

W. H. Orrick, being first duly sworn, says that he is one of the counsel of record in the above entitled

cause; that as such counsel he is authorized to verify the foregoing petition for review; that he has read the said petition and is familiar with the statements therein contained and that the statements made are true to the best of his knowledge, information and belief.

W. H. ORRICK

Subscribed and sworn to before me this 29th day of December, 1943.

[Seal] ANNE F. SURFT

Notary Public in and for the City and County of San Francisco, State of California.

[Endorsed]: T.C.U.S. Filed Jan. 3, 1944. [52]

[Title of Tax Court and Cause.]

AFFIDAVIT OF SERVICE BY MAIL

State of California
City and County of San Francisco—ss.

E. J. Demings, being first duly sworn, deposes and says:

That he is a clerk in the employ of W. H. Orrick, Esq., one of the counsel representing petitioner in the above-entitled matter; that he is a citizen of the United States of America, over the age of twenty-one years and not a party to the within action.

That on the 5th day of January, 1944 he duly placed, in a sealed envelope addressed to J. P. Wenchell, Chief of Counsel, Bureau of Internal Revenue, Washington, D. C. a notice of the filing of

a Petition for Review by the United States Circuit Court of Appeals for the Ninth Circuit of the decision [53] of The Tax Court of the United States heretofore rendered in the above-entitled cause, to which was attached a conformed copy of said petition; that a copy of said notice is attached hereto; that on said date he duly placed said envelope containing said notice and said copy of said petition for review, with the required postage thereon duly prepaid, in the United States mail at San Francisco, California, and that on said date there was and is a regular communication by United States mail between the City and County of San Francisco and the City of Washington, D. C.

E. J. DEMINGS

Subscribed and sworn to before me this 11th day of February, 1944.

HAZEL E. THOMPSON,

Notary Public in and for the City and County of San Francisco, State of California.

My Commission Expires October 14, 1946.

[Endorsed]: T.C.U.S. Filed Feb. 1, 1944. [54]

[Title of Tax Court and Cause.]

PRAECIPE FOR RECORD

To the Clerk of The Tax Court of the United States:

You are requested to prepare and certify and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, with refer-

ence to the petition for review heretofore filed by petitioner in the above cause, a transcript of the record in the above cause prepared and transmitted as required by law and by the rules of said court and to include in said transcript of record the complete record and all the proceedings and evidence in the above cause, including, without limiting the generality of the foregoing, the following documents or certified copies thereof, to wit:

1. The docket entries of all proceedings before The Tax Court of the United States, formerly known as the "United States Board of Tax Appeals".

2. Pleadings before The Tax Court of the United States, formerly known as the "United States Board of Tax Appeals", as follows:

(a) Petition for redetermination.

(b) Answer of respondent. [55]

3. Stipulation as to evidence, dated January 30, 1943, with all exhibits attached thereto.

4. Transcript of proceedings before The Tax Court of the United States, formerly known as the "United States Board of Tax Appeals".

5. The findings of fact and opinion of The Tax Court of the United States, formerly known as the "United States Board of Tax Appeals".

6. Petitioner's stipulation as to respondent's computation.

7. Decision of The Tax Court of the United States, formerly known as the "United States Board of Tax Appeals".

8. Petition for review filed by the petitioner in the above cause.

9. This Praecipe.
10. Affidavit of mailing.

(s) W. H. ORRICK
(s) CHARLES L. BARNARD
Counsel for Petitioner.

[Endorsed]: T.C.U.S. Filed Feb. 1, 1944. [56]

[Title of Tax Court and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of The Tax Court of the United States do hereby certify that the foregoing pages, 1 to 56, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 16th day of February, 1944.

[Seal] B. D. GAMBLE, Clerk,
The Tax Court of the United States.

[Endorsed]: No. 10697. United States Circuit Court of Appeals for the Ninth Circuit. Amelia Davis Bloch, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review a Decision of The Tax Court of the United States.

Filed March 4, 1944.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

In the United States Circuit Court of Appeals for the Ninth Circuit

No. 10697

AMELIA DAVIS BLOCH,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

STATEMENT OF POINTS TO BE RELIED ON

To the United States Circuit Court of Appeals for the Ninth Circuit and the Honorable Judges thereof:

The Petitioner hereby states and sets forth the following as the points on which she intends to rely on the above entitled appeal:

1. The basis to Petitioner of the 212 common

shares of The Dow Chemical Company (hereinafter called "Dow"), sold by her in March, 1940 (the gain from which sale is the subject matter of the above entitled proceeding) is the same as the basis to Petitioner of the identical shares of Great Western Electro-Chemical Company (hereinafter called "Great Western") from which they were constituted and converted—i.e. for which they were exchanged—on the statutory merger of Great Western with and into Dow.

2. The Court below (viz: The Tax Court of the United States—formerly known as the Board of Tax Appeals) erred in holding that the basis to Petitioner of said 212 common shares of Dow is to be determined by dividing the total cost to Petitioner of the Great Western shares acquired by Petitioner at different times and at different prices by the total number of Dow shares received by her and then multiplying that amount by the Dow shares sold by petitioner.

3. On the effective date of the Agreement of Merger dated November 19, 1938, between Great Western and Dow and pursuant to the terms and provisions of said Agreement and the applicable provisions of law of the States of California and Michigan, the outstanding Great Western shares (including those held by Petitioner) were constituted and converted into Dow common shares on the basis of one Great Western preferred share, $20 par value into 3/16ths of one Dow common share and one Great Western common share without par value into one Dow common share. On and after

said effective date and by virtue of the foregoing, each outstanding stock certificate which immediately prior to said effective date represented Great Western preferred or common shares (including each such certificate held by Petitioner) thereupon represented respectively the Dow common shares into which such Great Western shares had been so constituted and converted.

4. Within the meaning of Section 113(a)(6) of the Internal Revenue Code, the constitution and conversion of Great Western shares into Dow common shares mentioned in paragraph 3 above was the "exchange" of Great Western shares for Dow shares on the "reorganization" of Great Western and Dow and, accordingly, under said Section 113(a)(6) the basis to Petitioner of the Dow shares, respectively represented on and after the effective date of said agreement of merger by each outstanding Great Western certificate held by Petitioner on said effective date was the same as the basis to Petitioner of the Great Western shares represented thereby immediately prior to said effective date.

5. The certificate exchange in 1939 was merely an exchange of certificates each representing Dow common shares and on such exchange the certificates received by Petitioner and the shares represented thereby can be identified with, and traced to, specific certificates surrendered by Petitioner on such exchange and the shares represented thereby.

6. Even though Petitioner be mistaken in her contention that under Section 113(a)(6) of the Internal Revenue Code, the "exchange" of Great

Western shares for Dow shares on the "reorganization" of Great Western and Dow was the constitution and conversion of Great Western shares into Dow shares on the effective date of the agreement of merger and it be held that the "exchange" within the meaning of said section was the certificate exchange in 1939, nevertheless, the basis to Petitioner of said 212 Dow common shares sold by her in March, 1940 is the same as the basis to Petitioner of the identical Great Western shares for which they were exchanged. On said certificate exchange, Petitioner exchanged specific Great Western certificates and the specific shares represented thereby for specific Dow certificates and the specific shares represented thereby and, accordingly, under said Section 113(a)(6), the basis to Petitioner of said 212 Dow common shares was the same as the basis to her of the specific shares for which they were so exchanged.

7. Each Great Western certificate immediately prior to the effective date of the aforesaid statutory merger between Dow and Great Western, represented Great Western preferred or common shares and on or after said effective date represented Dow common shares. The merger did not affect the basis of any such certificate or of the shares represented thereby. Accordingly, the basis to Petitioner of the Dow common shares represented on and after the effective date of said statutory merger by each such certificate held by Petitioner was the same as the basis to Petitioner of the Great Western shares

(preferred or common) represented by each such certificate immediately prior to said effective date.

8. On the statutory merger Great Western preferred and common shares were constituted and converted into Dow shares. Accordingly, the basis of each such Dow share was the same as the basis of the Great Western shares from which they were constituted and converted.

Respectfully submitted,

W. H. ORRICK
CHARLES L. BARNARD
Attorneys for Petitioner
405 Montgomery Street
San Francisco, 4, Calif.

[Endorsed]: Filed March 9, 1944. Paul P. O'Brien, Clerk.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 10696

LOUIS BLOCH,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

No. 10697

AMELIA DAVIS BLOCH,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

STIPULATION

It is hereby stipulated by and between the parties to the above entitled proceeding subject to the approval by the Court as follows:

1. That only the record in the case of Amelia Davis Bloch (Docket No. 10697) shall be printed and only said case shall be briefed and presented to the Court in argument for decision.

2. The decision of the Court in the case of Louis Bloch (Docket No. 10696) shall be stayed until the decision in said case of Amelia Davis Bloch (Docket No. 10697) becomes final within the meaning of

Section 1140 of the Internal Revenue Code, and after the decision in said case of Amelia Davis Bloch (Docket No. 10697) shall so become final, either party in the case of Louis Bloch (Docket No. 10696) may, upon regular notice to the other party and upon the basis of this stipulation and a certified copy of said final decision in the case of Louis Bloch (Docket No. 10696), apply for an order directing the entry in the case of Louis Bloch (Docket No. 10696) of judgment corresponding to the result in the case of Amelia Davis Bloch (Docket No. 10697).

W. H. ORRICK
CHAS. L. BARNARD
Attorneys for Petitioners
405 Montgomery Street
San Francisco, 4, Calif.
SAMUEL O. CLARK, JR.,
Assistant Attorney General,
Attorney for Respondent.

So Ordered:

FRANCIS A. GARRECHT
Judge of the above-entitled Court.

[Endorsed]: Filed March 28, 1944. Paul P. O'Brien, Clerk.

No. 10,697

United States Circuit Court of Appeals

For the Ninth Circuit

AMELIA DAVIS BLOCH,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONER'S OPENING BRIEF

W. H. ORRICK,
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PARKER PRINTING COMPANY, 545 SANSOME STREET, SAN FRANCISCO

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No. 10,697

United States Circuit Court of Appeals

For the Ninth Circuit

AMELIA DAVIS BLOCH,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITIONER'S OPENING BRIEF

I.

STATEMENT OF JURISDICTION

Petitioner, on August 21, 1942, filed her petition with The Tax Court of the United States (then known as the Board of Tax Appeals) for a redetermination of the deficiency determined against her by Respondent for the calendar year ended December 31, 1940, set forth in his notice of deficiency dated, and mailed to Petitioner on, May 26, 1942, and The Tax Court of the United States on October 5, 1943, entered its decision thereon adverse to Petitioner. Petitioner, on January 3, 1944, filed with the Tax Court her petition for the review of said decision by

the above entitled court. The Collection District in which Petitioner's return for said calendar year was filed is the First District of California. (Record,* pp. 1, 2, 3, 4, 10, 52.)

The jurisdiction of the Tax Court of said petition is established by Section 272 of the Internal Revenue Code. The jurisdiction of this Court to hear this appeal is established by Sections 1141 and 1142 of the Internal Revenue Code.

II.

STATEMENT OF CASE

The facts of this case have been stipulated by the parties by stipulation filed with the Tax Court on February 1, 1943. (Record, pp. 2, 18-40.) Petitioner, immediately prior to the statutory merger, hereinafter referred to, of Great Western Electro-Chemical Company, a California corporation (hereinafter called "Great Western") with and into The Dow Chemical Company, a Michigan corporation (hereinafter called "Dow") held 865 shares of the preferred stock, $20 par value, and 280 shares of the common stock, without par value, of Great Western, represented as follows:

> Certificates numbered P392-P398, inclusive, each representing 100 shares of preferred stock, $20 par value;
>
> Certificate numbered PL145 for 95 shares of preferred stock, $20 par value;
>
> Certificate numbered PL414 for 70 shares of preferred stock, $20 par value;

*All references herein to the Record are to the Printed Record.

Certificates numbered 273 and 274 each representing 100 shares of common stock, no par value;

Certificates numbered L261 and L1178 representing respectively 30 and 50 shares of common stock, without par value.

(Record, p. 20.)

Petitioner acquired said stock at various times and at various prices. (Record, pp. 18-20.)

On or before December 31, 1938, Great Western merged with and into Dow under the terms and conditions of an Agreement of Statutory Merger between said corporations dated November 19, 1938 and pursuant to the applicable provisions of law of the State of California and of the State of Michigan. (Record, p. 21.)

The Agreement of Statutory Merger provides that on the effective date thereof the Great Western stock (excepting such stock as was held by either Great Western or Dow) should constitute and be converted into Dow stock on the following basis, viz.: Each share of preferred stock, $20 par value, of Great Western into 3/16 of one full paid and non-assessable share of Dow common stock, without par value. Each share of common stock, without par value, of Great Western into one full paid and non-assessable share of Dow common stock, without par value. By virtue of Article III of said Agreement of Statutory Merger and the applicable provisions of law of the States of California and Michigan, on and after the effective date of said Agreement of Statutory Merger the aforementioned certificates represented the shares of Dow common stock, without par value, which said Great Western stock con-

stituted and into which they had been converted. (Record, pp. 28-29.)

Under date of January 24, 1939, Petitioner forwarded to the Cleveland Trust Company the above described certificates. The Cleveland Trust Company cancelled said certificates so forwarded by Petitioner and issued to Petitioner in lieu thereof the following numbered certificates of Dow respectively in lieu of the said certificates so forwarded by Petitioner:

Dow Certificates Issued	*Dow Common Shares Represented Thereby*	*Great Western Certificates Cancelled*
C5822	100 shares)	(P392-398
C18244	62 shares)	(PL145
CLF171	3/16ths)	(PL414
C5823	100 shares	273
C5824	100 shares	274
C018245	50 shares)	(L261
	)	(L1178

(Record, p. 22.)

In March 1940 Petitioner sold 212 shares of Dow common stock for a total selling price of $33,264.24, 100 of which said 212 shares were represented by said Dow certificate numbered C5822, 62 of said 212 shares were represented by said Dow certificate numbered C018244, and 50 of said 212 shares were represented by said Dow certificate numbered C018245, acquired as aforesaid. (Record, p. 22.)

The question involved herein is as to the proper method for the determination of the basis of the Dow common stock to be used for determining the amount of gain or

loss realized on said sale. It is conceded by the parties, and was held by the Tax Court (Record, p. 48) that said shares of Dow common stock were acquired by Petitioner on a "tax-free" exchange or "reorganization" (of Great Western and Dow) as defined in Section 112(g)(1) of the Internal Revenue Code* and that the basis of said shares is governed by Section 113(a)(6) of the Internal Revenue Code. Petitioner claims that under Section 113(a)(6) the basis of the shares of Dow common stock sold is the same as the basis to her of the identical shares of Great Western stock, which said shares of Dow common stock constituted and from which they were converted—i.e., for which they were received in exchange—on the statutory merger of the Great Western with and into Dow. The Commissioner claims that while there is identification between the Great Western certificates surrendered and the Dow certificates received on the exchange, nevertheless Petitioner is not entitled to so trace the basis of the Dow stock to, and to identify it with, the basis of the Great Western stock but that under Section 113(a)(6) said basis in this case is to be determined by dividing the total cost of all shares of Great Western stock held by Petitioner at the time of the statutory merger by the number of shares of Dow common stock received on the exchange.

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*The instant transactions commenced prior to December 31, 1938. However, the applicable provisions of the Internal Revenue Code are identical with the corresponding provisions of the Revenue Act of 1938.

III.

SPECIFICATION OF ERRORS

A. The Tax Court erred in holding that the basis to Petitioner of said 212 shares of Dow common stock sold by her in March 1940 is to be determined by dividing the total cost to Petitioner of the shares of Great Western stock acquired by her at different times and at different prices by the total number of shares of Dow common stock received by her and in not holding that the basis of said 212 shares of Dow common stock is the same as the basis to Petitioner of the identical shares of Great Western stock which said shares of Dow common stock constituted and from which they were converted—i.e., for which they were exchanged on the statutory merger of Great Western with and into Dow.

B. The Tax Court erred in holding that the basis to Petitioner of the Dow common stock acquired by her on the statutory merger of Great Western with and into Dow was to be determined by dividing the total cost of the Great Western stock held by her by the number of shares of Dow common stock acquired on the merger.

C. The Tax Court erred in failing to hold that under Section 113(a)(6) of the Internal Revenue Code the basis of the Dow stock acquired on the statutory merger of Great Western with and into Dow is the same as the basis of the Great Western stock which it constituted and from which it was converted on the said statutory merger.

D. The Tax Court erred in holding that notwithstanding the identification between the Dow certificates received and the Great Western certificates surrendered in the

exchange that the basis of the Dow stock sold was to be determined by dividing the total cost of Great Western stock surrendered by the number of shares of Dow stock received.

E. The Tax Court erred in failing to hold that under Section 113(a)(6) of the Internal Revenue Code in view of the identification between the Great Western certificates surrendered and the Dow certificates received that the basis of the Dow stock sold was the same as the identical stock for which it was exchanged.

F. If the opinion of the Tax Court can be construed as finding that in 1939, and not in 1938, Petitioner received the shares of Dow common stock in question in exchange for shares of Great Western stock held by her, then such finding is erroneous and in conflict with the stipulation of the parties. The Great Western stock was constituted and converted into—i.e., exchanged for—Dow common stock on the effective date of the statutory merger of Great Western with and into Dow and said statutory merger took place on or before December 31, 1938. (Record, pp. 21, 28.) In 1939 there was merely an exchange of certificates each representing Dow common stock. (Record, p. 22.)

IV.

SUMMARY OF ARGUMENT

Petitioner in support of her position relies on the following points:

A. For convenience, the instant transaction may be regarded as comprising two exchanges, viz.: First, the constitution and conversion, pursuant to law, of Great Western stock—i.e., exchange for—Dow stock, on the effective date of the Statutory Merger which occurred on or prior to December 31, 1938; and, second, the 1939 Certificate Exchange. It is the basis of the Dow stock acquired on the First Exchange which is governed by Section 113(a)(6) of the Internal Revenue Code.

B. On the First Exchange, pursuant to law, each share of Great Western stock was constituted and converted—i.e., exchanged for—a share or fractional share of Dow common stock. Each Great Western share is identical, by operation of law, with the share or fractional Dow share which it constituted and into which it was converted on the Merger. Accordingly, for each of these reasons under Section 113(a)(6) of the Internal Revenue Code, the basis of each share or fractional share of Dow common stock so acquired is the same as the identical share of Great Western stock which it constituted and from which it was converted on the First Exchange.

C. On the Second Exchange there was identification between the certificates surrendered and the certificates received and accordingly the basis of the certificates received and the stock represented thereby may be identified with and traced to the certificates surrendered and stock represented thereby.

D. The rule that on a "tax-free" exchange the basis of the stock acquired is determined by dividing the total cost of the stock surrendered by the number of shares acquired is inapplicable where there is identification between the certificates sold. In the instant case there was identification between the certificates acquired and the certificates surrendered.

V.

ARGUMENT

A. Governing Statutory Provisions and Regulations.

As above set forth, it is conceded by the parties, and was held by the Tax Court, that the Dow common stock sold by Petitioner was acquired by her for Great Western stock on a so-called "tax-free" exchange and on a "reorganization" (of Great Western and Dow) as defined in Section 112(g)(1) of the Internal Revenue Code and the basis of the Dow common stock sold is governed by Section 113(a)(6) of the Internal Revenue Code providing generally for the basis of property acquired on a "tax-free" exchange. (Record, p. 48.)

Section 112(g)(1) defines the term "reorganization" and clause (A) of the definition includes a "statutory merger." Section 112(b)(3) of the Internal Revenue Code provides that the exchange of stock on a "reorganization" shall be "tax-free." Section 113(a)(6) prescribes generally the basis of property acquired on such a "tax-free" exchange.

Section 112(g)(1) provides:

> "Section 112(g). Definition of Reorganization. As used in this Section . . . and in Section 113 . . .—

(1) The term 'reorganization' means (A) a statutory merger or consolidation . . ."

Section 112(b)(3) provides:

"Section 112(b)(3). Stock for Stock on Reorganization. No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization."

Section 113(a)(6) provides:

"Sec. 113. Adjusted Basis for Determining Gain or Loss.

(a) Basis (Unadjusted) of Property.—The basis of property shall be the cost of such property; except that—

* * * * * * *

(6) Tax-free exchanges generally.—If the property was acquired, after February 28, 1913, upon an exchange described in Section 112(b) to (e), inclusive, the basis (except as provided in paragraphs (15), (17), or (18), of this subsection) *shall be the same as in the case of the property exchanged,* decreased in the amount of any money received by the taxpayer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. * * *" (Italics supplied.)

Under the Regulations:*

*The provisions here quoted from Regulations 111 are identical with the corresponding provisions of Regulations 101 and 103 which were in effect when the instant transactions occurred.

(i) Great Western is, and Dow is, a "party to the reorganization" of Great Western and Dow within the meaning of Section 112(b)(3). (Regulations 111, Sec. 29.112 (g)-2.) The regulation provides "Both corporations are parties to the reorganization if under statutory authority corporation A is merged into corporation B; . . ."

(ii) The "plan of reorganization" referred to in Section 112(b)(3) as applied to the instant case is the "statutory merger" of Great Western and Dow. See Regulations 111, Sec. 29.112(g)-2 which states that the "term 'plan of reorganization' refers to the consummated transaction specifically defined as a reorganization under Section 112(g)(1)" —i.e., in this case the "statutory merger" of Great Western and Dow.

Accordingly under Section 112(b)(3) the "exchange of Great Western stock for Dow common stock on the "statutory merger" of Great Western is "tax-free" and the basis of the Dow common stock acquired on this exchange is governed by Section 113(a)(6).

B. For Convenience, the Instant Transaction May Be Regarded as Comprising Two Exchanges, viz.: First, the Constitution and Conversion, Pursuant to Law, of Great Western Stock—i.e. Exchange for—Dow Stock, on the Effective Date of the Statutory Merger Which Occurred on or Prior to December 31, 1938; and, Second, the 1939 Certificate Exchange. It Is the Basis of the Dow Stock Acquired on the First Exchange Which Is Governed by Section 113(a)(6) of the Internal Revenue Code.

For convenience, the instant transaction may be regarded as comprising two exchanges, viz:

First Exchange. On the effective date of the statutory merger of Great Western with and into Dow (which according to the stipulation of the parties occurred on or

prior to December 31, 1938) the Great Western stock held by Petitioner immediately prior thereto constituted and was converted into Dow common stock pursuant to the provisions of said Agreement of Statutory Merger and the applicable provisions of law of the States of California and Michigan.

As above pointed out, Article III of the Agreement of Statutory Merger provides that on the effective date of the statutory merger each share of Great Western preferred stock should constitute and be converted into 3/16 of one share of Dow common stock and each share of Great Western common stock should constitute and be converted into one share of Dow common stock. The inclusion of this provision for conversion in the Agreement of Statutory Merger was required by the laws of the States of California and Michigan. See

California Civil Code, Sections 361, 361a;
Michigan General Corporation Act, Section 52.

Pursuant to this provision of the Agreement of Statutory Merger and in accordance with said provisions of law, on the effective date of said Agreement (which occurred on or prior to December 31, 1938) the Great Western stock in accordance with the terms of said Agreement constituted and was converted into—i.e., exchanged for—Dow common stock and on and after said effective date the Great Western stockholders became and were common stockholders and the Great Western certificates represented Dow common stock.

Copland v. Minong Mining Co. (1875), 33 Mich. 2;
Ridgway v. Griswold (1878) (C.C.D. Kansas), 20 Fed. Cases, Case No. 11,819.

See, also, *National Supply Co. v. Leland Stanford Junior University* (C.C.A. 9th Cir., 1943), 134 Fed.(2d) 689, certiorari denied, 1943, 320 U.S. 773, in which this Court held that shares acquired on a statutory consolidation did not involve the sale of securities under the Securities Act of 1933.

Second Exchange. In January 1939 Petitioner exchanged Great Western certificates which then represented Dow common stock for Dow certificates likewise representing Dow common stock.

This Second Exchange was a mere exchange of pieces of paper without any real legal significance. Even without the exchange of the physical certificates the old Great Western certificates automatically, from and after the effective date of the merger, represented and would have continued to represent Dow common stock. It is only the First Exchange that has any true legal significance. It is an essential characteristic of a statutory merger that immediately and automatically, by operation of law—or by legal fiction—the old Great Western shares were, at the moment the merger became effective, transmuted or transmogrified into Dow common stock, and this regardless of any exchange of physical certificates. It is immaterial whether the Second Exchange or "paper exchange" of the certificates occurs at or near the First Exchange or even years thereafter, since, from the moment of the effective date of the merger, the old Great Western certificates thereafter represented Dow common stock. The Second Exchange is required only for practical purposes and as a matter of record.

It is clear, therefore, as is set forth in the Specifications of Error that if the opinion of the Tax Court can be construed as finding that in 1939 and not in 1938 Petitioner received the Dow common stock in exchange for Great Western stock held by her then such finding is erroneous and in conflict with the stipulation of the parties.*

It is the First Exchange, and not the Second Exchange, which is the "tax-free" exchange to which Section 112(b)(3) of the Internal Revenue Code is applicable, and it is the Dow common stock acquired on the First Exchange and not the Dow certificates acquired on the Second Exchange which is the property the basis of which is prescribed by said Section 113(a)(6) of the Internal Revenue Code. It is the First Exchange which took place on the effective date, and was a part of the "statutory merger" (i.e., "reorganization") of Great Western and Dow. As above stated, under Section 112(b)(3) the exchange, on the "statutory merger," of Great Western stock for Dow stock is made "tax-free" and Section 113(a)(6) governs the basis of the stock acquired on this "tax-free" exchange. The Second Exchange was merely an exchange of certificates each then representing the same kind of stock, viz: Dow common stock.

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*The objectionable language in the opinion of the Tax Court is as follows: "There is no question but that the Dow shares were received by the petitioners in 1939 upon a reorganization under Section 112(g)(1) I.R.C." (Record, p. 48.) It is not clear whether by this statement the Tax Court intended to find that the Dow shares were received by Petitioner in 1939 or whether 1939 was merely referred to, in passing, as the year in which petitioner acquired the Dow certificates.

C. On the First Exchange, Pursuant to Law, Each Share of Great Western Stock Was Constituted and Converted—i.e., Exchanged for—a Share or Fractional Share of Dow Common Stock. Each Great Western Share Is Identical, By Operation of Law, With the Share or Fractional Dow Share Which It Constituted and Into Which It Was Converted on the Merger. Accordingly For Each of these Reasons Under Section 113(a)(6) of the Internal Revenue Code, the Basis of Each Share or Fractional Share of Dow Common Stock so Acquired Is the Same as the Identical Share of Great Western Stock Which It Constituted and From Which It Was Converted on the First Exchange.

Section 113(a)(6) of the Internal Revenue Code provides that the basis of the property acquired on the exchange "*shall be the same as in the case of the property exchanged.*" In the instant transaction under the provisions of the Agreement of Statutory Merger and the applicable laws of the States of California and Michigan, on the First Exchange *each* share of Great Western preferred stock was constituted and converted into—i.e., exchanged for—3/16 of one share of Dow common stock and *each* share of Great Western common stock was constituted and converted into—i.e., exchanged for—one share of Dow common stock.

In other words, by virtue of the provisions of the Agreement of Statutory Merger and the applicable provisions of law of the States of California and Michigan, there was a separate and distinct exchange of each share of Great Western stock for the share or fractional share of Dow common stock which it constituted and into which it was converted on the First Exchange. (See supra, pp. 12-13 for cases holding that on the effective date of the statutory merger the shares of a merging corporation constituted

and are converted into shares of the surviving corporation.) Furthermore, the Great Western stock represented by each Great Western certificate immediately prior to the First Exchange was constituted and converted—i.e., exchanged for—the Dow common stock represented by such certificate on and after the First Exchange. This Court and the Court below in applying Section 113(a)(6) of the Internal Revenue Code are bound by local law as to matters of this kind and accordingly must treat each such separate constitution and conversion as a separate exchange.

Burnet v. Harmel (1932), 287 U.S. 103;
Bankers Pocahontas Coal Co. v. Burnet (1932), 287 U.S. 308;
Burk-Waggoner Oil Association v. Hopkins (1925), 269 U.S. 110;
Helvering v. Metropolitan Edison Company (1939) 306 U.S. 522;
U. S. v. Seattle-First National Bank (1944) 88 L.Ed. (Adv. Op.) 593, 64 Sup.Ct. 713.

See, also, *National Supply Co. v. Leland Stanford Junior University,* supra.

Under Section 113(a)(6) the basis of the property acquired on the exchange is *"the same as in case of the property exchanged"*. Therefore, under Section 113(a)(6) the basis of each share and fractional share of Dow common stock thus acquired is the same as the identical share of Great Western stock which it constituted and from which it was converted (i.e., for which it was received in exchange) on the First Exchange and the basis of the Dow

common stock represented by each Great Western certificate on and after the First Exchange is the same as the Great Western stock represented by said certificate immediately prior to the First Exchange.

Cf. *Fuller v. Commissioner* (C.C.A. 1st, 1936) 81 F.(2) 176.

The application of any other rule in this case would lead to the strange and unusual result that the basis of each Great Western certificate held by Petitioner was, on the effective date of the merger, changed from its original basis to some other basis. Certainly the Court should not reach any such conclusion in the absence of strong and persuasive language compelling it so to do. Cf. *Helvering v. Rankin* (1935), 295 U.S. 123, 129, et seq.

The Tax Court held that the basis of the Dow common stock sold was to be determined by dividing the total cost of the Great Western stock by the number of shares of Dow stock received and in support of this ruling cited the following cases:

Commissioner v. Oliver (C.C.A. 3rd Cir., 1935), 78 Fed. (2d) 561;

Helvering v. Stifel (C.C.A. 4th Cir., 1935), 75 Fed. (2d) 583;

Commissioner v. Von Gunten (C.C.A. 6th Cir., 1935), 76 Fed.(2d) 670;

Commissioner v. Bolender (C.C.A. 7th Cir., 1936), 82 Fed.(2d) 591;

Arrott v. Commissioner of Internal Revenue (C.C.A. 3d—1943), 136 Fed.(2d) 449;

Rauol H. Fleischmann v. Commissioner (1939), 40 B.T.A. 672.

These cases arose under Section 113(a)(6) of the Internal Revenue Code (or its corresponding section in the prior Revenue Acts) and involved "tax-free" exchanges, under Section 112(b)(3), of the stock of one corporation for the stock of another corporation in connection with the acquisition by the second named corporation of the assets of the first named corporation in a "reorganization" as defined by Section 112(g)(1). These cases did not involve a statutory merger of one corporation with and into the other but a simple transfer of assets by one corporation to the other. In these cases it was held that the basis of each share of stock acquired was to be determined by dividing the aggregate cost of the stock surrendered by the number of shares acquired. Conceding solely for the purpose of argument under this point, that the rule of these cases is applicable where there has been identification on a voluntary exchange of certificates (with which position we will take issue under point E below) such rule is not applicable in the case of a statutory merger for the reasons above stated, viz:—On a statutory merger there is a separate and direct exchange, pursuant to law, of each share of the merging corporation for the share or fractional share of the surviving corporation which it constituted and into which it was converted on the merger. The Federal Court in applying Section 113(a)(6) must give effect to this provision of law and accordingly hold that the basis of each such share or fractional share of the surviving corporation (in this case-Dow) is the same as the basis of the individual share of the merging corporation (in this case—Great Western) which it constituted and from which it was converted on the effective date of the merger.

Furthermore, in view of the identity arising by operation of law, between each Great Western share and the share or fractional share of Dow which it constituted and into which it was converted on the merger, the rule of the cases relied on by the Tax Court is inapplicable and the instant case comes instead within the rule applicable to a "recapitalization" under which "identification" is permitted. It is well established that the rule of the cases relied on by the Tax Court do not apply to stock acquired on a "recapitalization" of a corporation.

Kraus v. Commissioner (C.C.A. 2d—1937), 88 Fed. (2d) 616;
Fuller v. Commissioner (C.C.A. 1st—1936), 81 Fed. (2d) 176.

In the *Kraus* and *Fuller* cases there was a stock split-up. In both the *Kraus* and *Fuller* cases, there was a "reorganization" under Section 112(g)(1), the exchange on the split-up was a "tax-free" exchange under Section 112(b)(3), and the basis of the stock acquired on the split-up was governed by Section 113(a)(6).

In the *Kraus* case, the "first-in first-out" rule was applied because there was no identification of the stock sold. In the *Fuller* case identification of the stock sold was proved and identification was allowed. In both cases, the Court refused to apply the rule applied by the Tax Court in this case, viz: that the basis of the stock acquired on a "tax-free" exchange is determined by dividing the total cost of the stock exchanged by the number of shares received, but held that in such cases the general rules for determining basis of stock on an exchange (i.e., the "first-in first-out" rule and the "identifica-

tion'' rule) were applicable. The basis of the rule of the *Kraus* and *Fuller* cases is the *identity* of the shares acquired on the ''recapitalization'' or split-up with the original shares which had been split up.

Kraus v. Commissioner, supra, 88 Fed.(2d) 616, at 618;

Fuller v. Commissioner, supra, 81 Fed.(2d) 176, at 178.

It is clear that the instant case comes within the rule laid down by the *Kraus* and *Fuller* cases. As above stated, there is a direct identity between the Great Western stock held by Petitioner immediately prior to the First Exchange and the Dow common stock acquired by her on the First Exchange. Pursuant to the Agreement of Statutory Merger and the applicable laws of the States of California and Michigan, each share of Great Western stock was constituted and converted a share or fraction of share of Dow common stock.

In the *Kraus* and *Fuller* cases and in the instant case this identity between the shares of Great Western (the merging corporation) and the shares of Dow (the surviving corporation) is established by operation of law. Cf. *U. S. v. Seattle-First National Bank* (1944), 320 U.S. 723, holding that on a statutory consolidation a transfer of stock was by operation of law and a transfer of real property was effectuated by virtue of the statute prescribing for consolidations.

See also:

Copland v. Minong Mining Co., supra;

Ridgway v. Griswold, supra.

There is certainly just as much identity between the shares of the merging corporation and the shares of the surviving corporation on a statutory merger as there is between the original shares and the new shares on a stock split-up.

Furthermore, by virtue of the laws of the States of California and Michigan the corporate identity of Great Western was "merged into" the corporate identity of Dow.

> *California Civil Code,* Sections 361, 361a;
> *Michigan General Corporation Act,* Sec. 53.

The courts, in tax and other kindred cases, have given effect to this continuance of corporate identity on a statutory merger and consolidation.

In the case of *Helvering v. Metropolitan Edison Company* (1939), 306 U.S. 522, which arose under the income tax law, the United States Supreme Court held that the surviving corporation on a statutory merger or consolidation is entitled to use the unamortized bond discount of a merging or consolidating corporation but that the corporation which merely acquired the assets of another corporation is not entitled to use such amortized bond discount of the transferee corporation.

In *U. S. v. Seattle-First National Bank,* supra, which arose under the Stamp Tax law, the United States Supreme Court held that in a statutory consolidation the consolidated corporation acquired the assets of a consolidating corporation by virtue of the provisions of law and that such acquisition was effectuated without the necessity of any deed, instrument or writing.

In *National Supply Co. v. Leland Stanford Junior University,* supra, this Court held that the issuance of stock

on a statutory merger or consolidation was not a sale under the Securities Act of 1933.

In view of this identity between the shares of Dow common stock held by Petitioner on and after the First Exchange and the Great Western stock held by her immediately prior to the First Exchange and the corporate identity between Great Western and Dow, it is clear that the rule laid down by the *Kraus* and *Fuller* cases is applicable in the instant case and that accordingly the basis of the Dow stock acquired is the same as the basis of the Great Western stock from which it was converted on the First Exchange.

We have shown that:

(i) On the First Exchange there was a separate exchange, pursuant to law, of each share of Great Western stock for the share or fractional share of Dow stock which it constituted and into which it was converted on the merger.

(ii) There is identity by operation of law between each share of Great Western stock and the share or fractional share of Dow stock which it constituted and into which it was converted on the merger. By operation of law the corporate identity of Great Western has been merged into the corporate identity of Dow. The rule of the *Kraus* and *Fuller* cases is therefore applicable.

Therefore under Section 113(a)(6) of the Internal Revenue Code for each of these reasons the basis of the Dow share sold is the same as the basis of the identical Great Western shares which they constituted and from which they were converted on the statutory merger.

D. On the Second Exchange There Was Identification Between the Certificates Surrendered and the Certificates Received and Accordingly the Basis of the Certificates Received and the Stock Represented Thereby May Be Identified With and Traced to the Certificates Surrendered and Stock Represented Thereby.

As above set forth, at the time of the Second Exchange the Great Western certificates surrendered then represented Dow common stock. This exchange was just like any other exchange of certificates of stock of the same corporation. It has been stipulated between the parties that there is identification between the certificates surrendered and the certificates received on the Second Exchange. (Record, p. 22.)

It is clear, therefore, that under the decisions the basis of the certificates received on such exchange and the stock represented thereby may be identified with and traced to the basis of the certificates surrendered on said exchange and the stock represented thereby.

Helvering v. Rankin, supra;
Davidson v. Commissioner (1938), 305 U.S. 44;
Fuller v. Commissioner, supra.

In view of the foregoing, we have shown that on the First Exchange under Section 113(a)(6) the basis of the common stock acquired is the same as the identical Great Western stock from which it was converted on said Exchange. We have also shown that the basis of the Dow certificates acquired on the Second Exchange and the Dow common stock represented thereby may be traced to and identified with the basis of the Great Western certificates surrendered on said Exchange and the Dow common stock represented thereby. In this case, the taxpayer sold Dow

certificates acquired on the Second Exchange. Petitioner has thus established the requisite identity between the Dow stock sold and Great Western certificates and stock acquired by her and accordingly the basis of the said Dow common stock is the same as the basis of the Great Western stock from which it was converted.

In our argument thus far we have conceded solely for the purposes of the argument that the rule that the basis of stock acquired on a "tax-free" exchange is determined by dividing the total cost of the stock surrendered by the number of shares acquired, is applicable in cases (such as the present one) where there is identification between the certificates surrendered and the certificates received on the exchange. Petitioner will now present, under point *E,* as an additional ground in support of her position that this general rule is not applicable in cases where, as here, there is identification between the certificates received and the certificates surrendered on a "tax-free" exchange. Accordingly, even though the arguments advanced under points *B* and *C,* above, be overruled by the Court, nevertheless, the Court must hold that the basis to Petitioner of the Dow common stock sold by her is the same as the basis to Petitioner of the identical Great Western stock for which they were exchanged.

E. The Rule That on a "Tax-Free" Exchange the Basis of the Stock Acquired Is Determined by Dividing the Total Cost of the Stock Surrendered by the Number of Shares Acquired Is Inapplicable Where There Is Identification Between the Certificates Sold. In the Instant Case There Was Identification Between the Certificates Acquired and the Certificates Surrendered.

With the exception of the case of *Rauol H. Fleischmann v. Commissioner* (1939), 40 B.T.A. 672, the cases cited by the Tax Court in its decision dealt with certificate exchanges on "tax-free" "reorganizations" where there was no identification between the certificates acquired and the certificates surrendered. It was held that under such circumstances the so-called "first-in first-out" rule now set forth in Regulations 111, Sec. 19.22(a)-8, was inapplicable. It was pointed out that under this Regulation the "first-in first-out" rule is applicable only to stock which is acquired at *different times* and that on a "tax-free" exchange the stock is acquired at the same time. It was accordingly held in these cases that under Section 113(a)(6), in the absence of identification, the basis of stock acquired on the exchange was determined by dividing the cost of the stock surrendered by the number of shares received.

Commissioner v. Oliver, supra, 78 Fed.(2d) 561, at 562;

Helvering v. Stifel, supra, 75 Fed.(2d) 583, at 584;

Commissioner v. Von Gunten, supra, 76 Fed.(2d) 670, at 671;

Commissioner v. Bolender, supra, 82 Fed.(2d) 591, at 592;

Arrott v. Commissioner of Internal Revenue, supra, 136 Fed.(2d) 449, at 451.

Under such circumstances no other rule could have been applied. The only three possible bases are, (i) a basis determined by identification; (ii) a basis determined by some statutory or administrative rule such as "first-in first-out"; and (iii) a basis determined by averaging such as applied in these cases. Clearly, if there is no identification and no administrative or statutory rule is applicable, the only rule that can be applied is the "average cost rule" which was used.

In the *Fleischmann* case, supra, the Board of Tax Appeals extended the rule of these cases to a situation where identification between the certificates surrendered and the certificates acquired on the exchange had been established. It is this extended rule which the Tax Court purported to apply in the instant case. It is respectfully submitted that the rule of the *Fleischmann* case cannot be supported. Section 113(a)(6) (which controls the *Fleischmann* case and controls the instant case) provides that the basis of the property acquired on the exchange "shall be the same as the basis of the property exchanged." If, as in the *Fleischmann* case and in the instant case, the taxpayer has shown that specific certificates surrendered were exchanged for specific certificates acquired, then under Section 113(a)(6) the basis of each such certificate thus acquired must be the same as the basis of the certificate for which it was surrendered. The "first-in first-out" rule and the "average cost rule" are arbitrary rules and these rules should be applied only in the absence of identification.

Helvering v. Rankin (1935), 295 U.S. 123.

In this case the Court held that identification of shares sold could be established by "intention" and that the "first-in first-out" regulation was inapplicable, which such intention had been shown and in answer to a claim that the "first-in first-out" regulation was invalid, said (p. 129 et seq.):

> "The validity of the regulation, thus construed, cannot seriously be questioned. The contention advanced by the taxpayers, both here and in the companion case of Snyder v. Commissioner of Internal Revenue, 295 U.S. 134, 55 S.Ct. 737, that the regulation, as applied to marginal transactions, is invalid under the Fifth Amendment, because it creates a conclusive presumption, must rest wholly on the assumption that the shares traded on margin are incapable of identification. Since that assumption is erroneous, it is clear that no conclusive presumption is established. It is, at most, the burden of proof that is affected. For the margin trader, while being required to establish the identity of the shares, in order to avoid the 'First-in, first-out' rule, is left free to introduce any relevant evidence. *Nor is he arbitrarily deprived of any of the important attributes of ownership, such as the 'right to decide which stock he is going to sell.'* Indeed it is conceded, at least by the taxpayer in this case, that the regulation, as we now interpret it, 'provides a useful and reasonable rule for ascertaining what stock was sold in cases where there is no proof, or lack of satisfactory proof, of the fact.'" (Italics supplied)

In the instant case it has been stipulated by the parties that such identification between the certificates surrendered and the certificates received exists. Accordingly, under the additional argument presented under this point *E*,

even though the Petitioner be mistaken in the position urged under points *B* and *C*, above, nevertheless, in view of such identification, the basis to the Petitioner of the Dow common stock sold must be held to be the same as the basis of the identical Great Western stock for which it was exchanged.

CONCLUSION

In view of the foregoing, it is respectfully submitted that the decision of the Tax Court should be reversed.

Respectfully submitted,

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No. 10697

In the United States Circuit Court of Appeals for the Ninth Circuit

AMELIA DAVIS BLOCH, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

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OPINION BELOW

The memorandum opinion of the Tax Court (R. 46–50) is not officially reported.

JURISDICTION

This case involves federal income tax for the calendar year 1940. On May 26, 1942, the Commissioner of Internal Revenue mailed to the taxpayer notice of a deficiency in tax for 1940 in the amount of $1,035.53. (R. 10–15.) Within 90 days thereafter and on August 21, 1942, the taxpayer filed a petition with the Tax Court (then the Board of Tax Appeals) for a redetermination of the deficiency under the provisions of Section 272 of the Internal Revenue Code. (R. 3–15.) The decision of the Tax Court finding a

deficiency in income tax of $932.75 for 1940 was entered October 5, 1943. (R. 52.) The case is brought to this Court by a petition for review filed January 3, 1944 (R. 52–57), pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code.

QUESTION PRESENTED

Whether under Section 113(a)(6) of the Internal Revenue Code the basis of shares of stock of Dow Chemical Company, sold by taxpayer in 1940, is properly determined by averaging the taxpayer's cost of shares of another corporation which taxpayer had previously exchanged for the Dow stock in a tax-free reorganization.

STATUTE INVOLVED

Internal Revenue Code:

> SEC. 112. RECOGNITION OF GAIN OR LOSS.
>
> * * * * *
>
> (b) *Exchanges Solely in Kind.*—
>
> * * * * *
>
> (3) *Stock for stock on reorganization.*—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corportion a party to the reorganization.
>
> * * * * *
>
> (g) *Definition of Reorganization.*—As used in this section and section 113—
>
> (1) The term "reorganization" means (a) a statutory merger or consolidation, * * *

(2) The term "a party to a reorganization" includes a corporation resulting from a reorganization and includes both corporations in the case of a reorganization resulting from the acquisition by one corporation of stock or properties of another.

* * * * *

(26 U. S. C. 1940 ed., Sec. 112)

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

* * * * *

(6) *Tax-free exchanges generally.*—If the property was acquired, after February 28, 1913, upon an exchange described in section 112 (b) to (e), inclusive, the basis (except as provided in paragraphs (15), (17), or (18) of this subsection) shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the taxpayer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. * * *

* * * * *

(26 U. S. C. 1940 ed., Sec. 113)

The corresponding provisions of the Revenue Act of 1938, c. 289, 52 Stat. 447, are identical.

STATEMENT

The facts were stipulated (R. 18–40) and may be summarized as follows:

During the years 1923 to 1938, inclusive, the taxpayer acquired at various times by purchase and through a recapitalization shares of preferred and common stock in Great Western Electro-Chemical Company (hereinafter referred to as "Great Western"). (R. 18–20.) Immediately prior to December 31, 1938, the taxpayer's stockholdings and costs thereof in Great Western were as follows (R. 18–20):

Stock	Certificate No.	Number of shares	Cost
6% Preferred; Par Value $20	P 392–398 (for 100 shares each)	700	$11,025.00
	PL 145	95	
	PL 414	70	1,583.75
Common; No Par Value	273–274 (for 100 shares each)	200	2,300.00
	L 261	30	
	L 1178	20	1,006.00
	Total cost		$15,914.75

By agreement of statutory merger dated November 19, 1938 (R. 23–35), it was provided that Great Western should be merged with the Dow Chemical Company, the merger to be effective when approved by the stockholders of each corporation and when the formalities required by statute for merger had been performed (R. 25–27, 33). Upon the effective date of the agreement each share of Great Western preferred stock was to constitute and be converted into three-sixteenths of a share of no par value common stock of Dow, and each share of Great Western common stock was to constitute and be converted into one share of no par value common stock of Dow. (R. 28–29.) It was provided that Dow would issue its certificates in exchange for Great Western stock on this basis, but that stockholders of Great Western who did not ap-

prove of the merger might demand the fair market value of their shares as provided by law. (R. 29.) It was further provided that upon the effective date of the agreement all of Great Western's property, rights, privileges, powers, and franchises, would henceforth be vested in Dow. (R. 31–32.)

On or before December 31, 1938, the merger of Great Western with Dow became effective (R. 21) and on January 11, 1939, Dow notified the shareholders of Great Western that they were entitled to receive certificates of Dow stock in the agreed ratio upon surrender for cancellation of the certificates representing their Great Western shares (R. 39–40).

On January 24, 1939, taxpayer forwarded all her Great Western certificates to the transfer agent, who cancelled them and issued to her certificates representing $162\frac{3}{16}$ shares of Dow stock in lieu of of the certificates for 865 shares of Great Western preferred stock; and certificates representing 250 shares of Dow stock in lieu of the certificates for 250 shares of Great Western common stock.[1] (R. 22.)

In March, 1940, taxpayer sold 212 shares of the Dow stock for a total selling price of $33,264.24. (R. 22.) The Tax Court found that the taxpayer's cost of the Great Western shares represented by the 212 shares of Dow stock sold was $13,900.17. She used this cost basis in determining the capital gain on the sale. (R. 47.)

[1] In the case of the common stock two certificates for 100 shares each of Dow stock were issued in lieu of two certificates for 100 shares each of Great Western and one certificate for 50 Dow shares was issued in lieu of two certificates for 30 and 20 shares, respectively, of Great Western common. (R. 22.)

In his deficiency notice the Commissioner determined that the taxpayer's cost of the 212 shares sold in 1940 was $8,185.32 and asserted a deficiency based in part on the increased capital gain on the sale resulting from this determination. (R. 12–13.) The Commissioner computed the $8,185.32 cost of the 212 shares by dividing the taxpayer's total cost of all Great Western shares acquired at different times and different prices by the total number of Dow shares received in exchange to get the cost per share, and then multiplying that amount by 212, the number of shares sold. (R. 47.) The Tax Court approved the Commissioner's determination of the cost basis.[2] (R. 50.)

SUMMARY OF ARGUMENT

Section 113 (a) (6) of the Internal Revenue Code provides that the cost basis of the shares of Dow Chemical Company acquired by taxpayer in a tax-free reorganization shall be the same as the Great Western stock for which they were exchanged. The Tax Court's holding that that basis under this statute is to be computed by averaging the cost of all the Great Western shares over the Dow shares acquired in exchange is correct. This method gives effect to reality. The Dow shares were all received at one time in one exchange and represent an equivalent

[2] The Tax Court consolidated the cases of taxpayer and her husband, involving the same question, for hearing and its opinion deals with both taxpayers. (R. 46–50.) It has been stipulated in this Court (R. 66–67) that the case of Louis Bloch shall be controlled by the final decision in the instant case.

interest in the new company. Each Dow share was received in exchange for the same number or numbers of Great Western shares, regardless of what the Great Western shares had cost the taxpayer. Consequently the assignment of an equal basis to each new Dow share conforms to the facts, and this is true whether the exchange of stock be considered voluntary or involuntary. The fact that stock of two corporations is involved in this case distinguishes it from cases involving stock split-ups in the same corporation, wherein it is held that the first-in, first-out rule is relevant for computing the basis of new shares.

The contention that each share of Great Western stock was separately exchanged for a share, or fraction of a share, of Dow stock is not supported by the merger agreement or by local law. Nor does Section 113 (a) (6) require that the transaction be viewed as a separate exchange of each Dow share for each Great Western share.

Under the rationale of the average method of determining the basis of stock in a new company, it is immaterial whether shares of the new stock can be identified with particular shares of stock of the old company. But in any event there has been no identification in this case. Each Dow share was exactly like every other Dow share and was indistinguishable from the others. Consequently it was impossible when they were all exchanged at one time to identify any Dow share with any Great Western share. The pairing up of certificate numbers is only an arbitrary

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device, not resting on any factual basis of identity, and fails to identify the shares represented by the certificates so matched.

In the present case, however, there was no pairing of particular certificate numbers in the case of the Dow shares issued in lieu of Great Western preferred shares, and hence no identification between those shares even through the device of matching. Although certificates were paired in the case of the Dow shares issued in lieu of the Great Western common shares, this was not shown to have been with intent to identify the shares represented by the certificates, and hence is without significance. But even if this arbitrary matching of certificates is held to constitute identification, there was at most identification of only a part of the Dow shares sold in 1940. The average cost rule must be used to compute the basis of shares not identified and should be used for all the shares, rather than a hybrid system of computing basis by two methods.

Nor has identification been made in this case by showing that the old and new shares were identical. The Dow shares represented interests in a new corporation possessing far greater assets than did the old corporation, and consequently they were not identical with the old shares. Further, although the exchange of stock was not made on a separate share for share basis as taxpayer contends, even if it had been so made, there is no evidence by which a particular share of new stock can be identified with a particular share of old stock.

ARGUMENT

Taxpayer's cost of the shares of stock of Dow Chemical Company is properly determined by the average cost method

The sole question in this case concerns the method by which the cost basis of the 212 shares of Dow stock sold by taxpayer in 1940 is to be determined. The shares sold were a part of the 412 3/16 shares of Dow stock acquired by taxpayer in exchange for all her stock in Great Western. It is not disputed that the exchange took place in connection with a statutory merger of Great Western and Dow and that this constituted a reorganization as defined in Section 112 (g) of the Revenue Act of 1938 and the Internal Revenue Code, *supra,* on which no gain or loss was recognized under Section 112 (b) (3) of the statute.[3] In such circumstances, Section 113 (a) (6) of the Internal Revenue Code, *supra,* provides that the basis of the property acquired—

> shall be the same as in the case of the property exchanged.

Thus, under the statute the 412 3/16 shares of Dow stock acquired in the reorganization must take the cost basis of the Great Western stock surrendered in exchange therefor, or $15,914.75. But since only 212 of the 412 3/16 shares were sold in 1940, the question arises as to what portion of the total cost of $15,914.75 is to be allocated to the 212 shares sold.

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[3] The provisions of the Revenue Act of 1938 control the year 1938, during which the merger occurred. The provisions of the Internal Revenue Code control the year 1939, during which the exchange of stock certificates was made. However, the sections of the two statutes which are involved in this case are identical in text.

The taxpayer contends that she has identified the Dow shares sold with particular shares of Great Western stock surrendered in exchange and that the basis of these Great Western shares carries over to the Dow shares. We contend that the Tax Court correctly held (R. 48–50) that the cost of the Dow shares sold in 1940 must be determined by the average cost method, regardless of whether the Dow shares were identified with any Great Western shares. We contend further that, in any event, no identification of the shares sold in 1940 was made.

1. The basis is determined by the average cost method irrespective of identification

It is apparent that the cost of a particular block or share of stock is difficult to determine when the owner of the stock has acquired a number of shares of that stock, all exactly alike except that they were acquired at different times and at different costs. In order to meet this difficulty, the Treasury in a long standing regulation [4] ruled that—

> If shares of stock in a corporation are sold from lots purchased at different dates or at different prices and the identity of the lots cannot be determined, the stock sold shall be charged against the earliest purchases of such stock.

See Treasury Regulations 103, promulgated under the Internal Revenue Code, Section 19.22 (a)–8. This is the familiar "first-in, first-out" rule, and it is to

[4] The regulation was first adopted in Article 4, paragraph 60, of Treasury Regulations 33 (Revised), promulgated under the Revenue Acts of 1916 and 1917.

be noted that it in terms applies only to purchases and sales of stock of a single corporation.

Nevertheless, the Commissioner sought to apply the first-in, first-out rule to cases wherein the original blocks of stock were exchanged for new stock in a tax-free reorganization. The courts, however, refused to apply the first-in, first-out rule in such circumstances. Commencing with *Commissioner* v. *Von Gunten,* 76 F. 2d 670 (C. C. A. 6th), it has been uniformly held that because shares received in a tax-free reorganization are shares in a new company which have all been received in one single transaction of exchange and for a single consideration, the shares of the old corporation, and because no particular share of the new stock acquired in this way represents any particular share of the old stock, the cost of the new shares is to be determined by dividing the total cost of all the old stock by the number of shares of the new stock. *Commissioner* v. *Stifel,* 75 F. 2d 583 (C. C. A. 4th); *Commissioner* v. *Oliver,* 78 F. 2d 561 (C. C. A. 3d); *Commissioner* v. *Bolender,* 82 F. 2d 591 (C. C. A. 7th); *Walker* v. *Commissioner,* 35 B. T. A. 640; *Epstein* v. *Commissioner,* 36 B. T. A. 109; *Runkle* v. *Commissioner,* 39 B. T. A. 458; *Fleischmann* v. *Commissioner,* 40 B. T. A. 672; *Mehan* v. *United States* (W. D. Mo.), decided September 3, 1937 (20 A. F. T. R. 1344).

There is some indication in the earlier cases cited that the use of the average cost method might not be proper if it were possible to identify particular new shares as having been exchanged for particular old

shares and in such case that the actual cost of the given block of shares of the old company might then be employed.[5] But in *Arrott* v. *Commissioner,* 136 F. 2d 449 (C. C. A. 3d), the court squarely held that where stock in a new company is acquired in exchange for stock in an old company in a tax-free reorganization, the average cost method is the only permissible rule for determining the cost of the new shares, regardless of whether identification of the new shares with the old is possible. It said (p. 452):

> We think it [the average cost rule] is the only sound rule. The old shares all have the same exchange value for the new ones no matter what they cost the taxpayer. He gets as much new stock for the share for which he paid $80 as he does for the share for which he paid $120. The old shares lose their identity when traded for the new, just as the money with which one buys a war bond loses its identity in the certificate, though to the purchaser some of it may have been a gift, some won on a horse race and the remainder earned by the sweat of his brow. The old shares are gone; the new shares in what is at least nominally a new company takes their place. Each new share costs the taxpayer the quotient of the sum of the cost of the old shares divided by the number of new shares he receives.

[5] It is significant, however, that in none of the cases considering the method of computing the basis of new shares exchanged for old in a reorganization has it been held that there was identification of the new shares with the old. And it will be developed, *infra*, that there was no identification in this case.

> If this is correct, the question of identification drops out of the operative facts in determining the value of shares received in a tax free reorganization. If it be thought to go too far, and identification of new shares received for specified old ones is legally relevant, it will not help the taxpayer here for there is no identification.

See also *Fleischmann* v. *Commissioner, supra,* where the Board of Tax Appeals indicated that even if it were possible to identify specific new shares with specific old shares, the application of the average cost method would not be avoided.

This rule is consistent with reality. After the merger the taxpayer had a certain number of Dow shares, received all at one time in exchange for her Great Western shares. Each share of each class of Great Western stock obtained for taxpayer the same share in the Dow enterprise, regardless of what that Great Western share had cost her. The only rational method then is to compute the cost of the Dow shares on an average basis. To assign different bases to shares which have the same value, represent equivalent interests, and were all acquired at one time would achieve an arbitrary, unreasonable, and unreal result.

The unreality is emphasized by the results obtained in this case under the two methods of computing basis. The total cost basis of the 412 3/16 shares of Dow stock was $15,914.75. Under the taxpayer's method a cost basis of $13,900.17 is assigned to 212 of those shares (an average of about $65.57), leaving

only $2,014.58 as the basis of the remaining 200$^{3}/_{16}$ shares (an average of about $10). Certainly it is arbitrary to say that, of a block of shares acquired in one transaction for one consideration, one-half have a basis of $65.57 and the other half one of $10. How much more reasonable it is to spread the consideration over all the shares equally, as is done by the average cost method, resulting in a uniform basis for all the shares of $38.61. (See R. 13.)

Taxpayer seeks to avoid the effect of the *Arrott* case by arguing (Br. 18) that the average cost rule is not applicable to cases of involuntary exchanges, such as she contends was involved in her case. In none of the cases deciding that the average cost method is proper for determining the basis of shares acquired in a reorganization exchange was the holding made to depend on whether the exchange was voluntarily or involuntarily made; and the rationale of the average cost rule is applicable to any exchange of stock in one corporation for stock in another, irrespective of the reason for the exchange. But in any event, taxpayer erroneously asserts that the exchange was involuntary in her case. The right was preserved to her by the agreement of merger (R. 29) and by law (Sec. 369, Civil Code of California (1941)) to demand and receive the fair market value of her Great Western stock if she did not approve of the merger. Thus she had an option to participate in the reorganization or to receive the value of her stock, and her election to become a share holder in the new company precludes the exchange from being an involuntary one.

Taxpayer also contends (Br. 19–20) that her case is controlled by *Kraus* v. *Commissioner,* 88 F. 2d 616 (C. C. A. 2d), and *Fuller* v. *Commissioner,* 81 F. 2d 176 (C. C. A. 1st). In those cases it was held that in the case of new stock acquired in a recapitalization the average method of determining cost was not proper and that cost was to be determined by reference to the first-in, first-out rule unless there was identification of new shares with old shares, in which case the new shares were to take the basis of the old.[6] There, however, the stockholder merely received new stock in the *same corporation* by reason of a stock split-up or reduction of stock, a situation which falls within the scope of the first-in, first-out regulation. In the *Kraus* case it was specifically pointed out (p. 618) that the fact that the stock of only one corporation was involved was sufficient to distinguish that case from cases where the stock of a new corporation was acquired in exchange for the old stock. Since the taxpayer's case involves the stock of *two* corporations, it is similarly distinguishable from the *Kraus* and *Fuller* cases and is controlled by the *Arrott, Von Gunten,* and similar cases, holding that the average method is proper for determining basis.

Taxpayer's principal argument appears to be that under the agreement of merger each old share of Great Western stock was separately exchanged for

[6] But see *contra Big Wolf Corp.* v. *Commissioner,* 2 T. C. 751, reviewed by the whole Tax Court, where the average method of determining the basis of new shares acquired in a recapitalization was held proper, since identification of the new shares was impossible.

each new share, or fraction thereof, of Dow stock (Br. 15–16) and hence (Br. 25–28) that Section 113 (a) (6) requires each new share to take the basis of each old share when identification between them has been established. This contention depends upon the identification of a specific new share with a particular old share, so that the actual cost of that new share may be known. It will be shown in the second division of this brief that taxpayer has not identified particular shares so that she must fail in this contention in any event. In the absence of specific identification, the actual cost of a particular share cannot be determined, and the average cost rule is the only method available by which the basis may be determined. But here it will be shown that the argument that each share was separately exchanged is without basis.[7]

It is true that the agreement of merger provides in Article III (R. 28–31) that on the effective date

[7] Taxpayer contends (Br. 16) that this Court is bound by local law to treat the transaction as though each share were separately exchanged. But taxpayer has not shown that local law regards the transaction as a series of separate exchanges. The statutes cited by her (Br. 12) contain no such provision, nor do *Copland* v. *Minong Mining Co.*, 33 Mich. 2, and *Ridgway* v. *Griswold*, Fed. Cases, No. 11819, so hold. Furthermore, even if the local law were as taxpayer contends, this is not a case where the federal courts would be bound thereby. The question here concerns the application of a taxing statute, whose operation is not dependent on state law. The exchange involved is factually essentially the same as other reorganization exchanges occurring in other states and must receive the same treatment under the federal basis statute, in order to give the statute uniform application. Cf. *Burnet* v. *Harmel*, 287 U. S. 103; *Burk-Waggoner Assn.* v. *Hopkins*, 269 U. S. 110.

of the merger the outstanding shares of Great Western are to constitute and be converted into Dow shares at fixed ratios (R. 28–29), but it does not provide that each share of old stock is to be separately exchanged for each share of new. On the contrary, it is clear that all shares are to be converted simultaneously on the date of the merger and the word "share" is used in the singular only to establish the rate of exchange. Certainly the conversion carried out in the exchange of certificates was not made share for share, but involved only one exchange, the shareholder's stock interest in the old corporation for his stock interest in the new.[8]

Section 113 (a) (6) does not provide that upon a single exchange of blocks of stock the basis of each new share shall be the same as that of the old. It provides only that the basis of property acquired on the exchange "shall be the same as in the case of the property exchanged." Consequently the provisions of the statute are served when the basis of all the

[8] Although the point does not appear to be material in the argument we take issue with the taxpayer's contention (Br. 11–14) that the merger transaction can be broken down into two separate exchanges. It is a basic principle in reorganization cases that the transaction must be reviewed as a whole and not be separated into its component steps. *Case* v. *Commissioner*, 103 F. 2d 283, 286 (C. C. A. 9th); *Bassick* v. *Commissioner*, 85 F. 2d 8 (C. C. A. 2d), certiorari denied, 299 U. S. 592, rehearing denied, 299 U. S. 623. Applying this principle, it is clear that there was only one exchange of shares in this case. Even though the assenting stockholders of the old company may have acquired an interest in the assets of the new corporation on the date of the merger, the old certificates did not represent this interest and the exchange was completed when the certificates evidencing shares of the new company were issued.

new stock acquired at one time and for a single consideration is assigned the basis of all the old stock, as was done in the *Arrott* case and by the Tax Court in the instant case.

Thus, upon the authority of the *Arrott* case, we submit that the taxpayer's basis for the shares sold in 1940 is to be determined by the average cost method, and that it is irrelevant whether the shares sold were identified with any particular old shares. But even though the matter of identification be regarded as pertinent, in the following section of the argument it will be shown that the evidence in this case fails to identify the new shares with the old. There can be no question that, if there was no identification of the shares sold with any particular old shares, the average cost method is proper for determining taxpayer's basis for the shares sold. All the cases so hold. See *Commissioner* v. *Von Gunten,* 76 F. 2d 670 (C. C. A. 6th); *Commissioner* v. *Stifel,* 75 F. 2d 583 (C. C. A. 4th); *Commissioner* v. *Bolender,* 82 F. 2d 591 (C. C. A. 7th); and other cases cited above.

2. Taxpayer's evidence fails to identify the shares sold in 1940 with any old shares

The problem has frequently arisen of whether stock has been sufficiently identified so as to avoid the application of the first-in, first-out rule and it has been held that identity may be established not only by means of certificate numbers but also by reference to the cost or date of acquisition of the stock. See, for example, *Helvering* v. *Rankin,* 295 U. S. 123;

Davidson v. *Commissioner*, 305 U. S. 44; *Rule* v. *Commissioner*, 127 F. 2d 979 (C. C. A. 10th); *Curtis* v. *Helvering*, 101 F. 2d 40 (C. C. A. 2d); *Kraus* v. *Commissioner, supra; Fuller* v. *Commissioner, supra.* But all of these cases involve the means of identifying shares in *one corporation* only, which the taxpayer has acquired at different times and prices. In such case, if he disposes of shares represented by a certain certificate number and can show that he acquired the shares represented by that certificate for a certain cost, he has sufficiently identified the stock sold and may use that cost as his basis.

However, in no case, so far as we have found, where there has been an intervening exchange of stock in one company for stock in another, so that the stock of two corporations is involved, has it been held that identity between the old and new stock has been established. Although the opinion in the *Arrott* case assumes that identification may be possible although it was not established in that case, we submit that identification of new shares with any particular old shares is incompatible with the nature of a reorganization exchange and hence is impossible. In any event, there was no identification here.

In a reorganization a stockholder does not receive certain new shares in exchange for certain old shares and other new shares for other old shares. On the contrary, he surrendered all his shares in the old company and receives shares in the new company all at one time in a single transaction. The new shares are received as a unit for a single consideration, the stock-

holder's entire interest in the old corporation. All the old shares represented the same interest in the old corporation's assets but may be distinguished by reference to the time or the price of acquisition. Each share in the new corporation also represents the same interest in the assets of that corporation but since the new shares are all acquired at one time for one consideration there is no way in which they may be distinguished; each new share is exactly like every other new share. Consequently, it is impossible to identify any new share with any old share, except on a purely arbitrary basis. The attempt to identify shares through matching certificate numbers, when all the shares are exchanged at one time, is only an arbitrary device and fails of real identification. For example, suppose that 20 shares of stock in Corporation A, represented by Certificate 1 for 10 shares which cost $100 and Certificate 2 for 10 shares which cost $200, are exchanged at one time for 20 shares of stock in Corporation B represented by Certificates 1 and 2 for 10 shares each. There is no more reason for matching Certificate 1 of Corporation B with Certificate 1 of Corporation A than there is for matching Certificate 2 of Corporation B with Certificate 1 of Corporation A, since the B shares represented by the two certificates are all identical and all issued at one time. Even though Certificate 1 be matched with Certificate 1, this can represent only an arbitrary choice and is not the result of actually identifying the shares represented thereby.

This was the view taken in *Crespi* v. *Commissioner,* 126 F. 2d 699 (C. C. A. 5th). There the charter of

a corporation had expired and a new corporation of the same name was formed to continue the same business. The taxpayer exchanged the stock held by him in the old corporation for an equivalent number of shares in the new corporation. Upon sale of some of the new shares, the court held that the cost basis for those shares must be computed by means of the average cost rule and not by using the cost basis of the old shares for which they were exchanged. This was true even though the corporation's records showed out of which old certificates the new certificates were issued, and each new certificate could be matched with the old certificate against which it was issued. The reasoning of the court was as follows (p. 701–702):

> When upon expiration of its charter the assets of the old corporation passed to its officers and directors as trustees, the full property in them passed to them as a whole, * * * When they were transferred to the new corporation the property was transferred, and had a value, as a whole, and when, to evidence the ownership of this value, shares in the new corporation were issued and distributed, each share represented an aliquot part of this value, and therefore each took the same basis as every other share.
>
> Despite therefore, the elaborate measures the taxpayer took to invest the new shares with the appearance of identity with the old, this was only appearance and it is not possible to affirm, as the taxpayer asks us to do, of a sale of shares in the new company, that the sale was not of an aliquot interest in that company as the owner

> of all the properties of its predecessor, but was a sale of shares representing and in law the same as, particular shares purchased in the old company.

Cf. also *Big Wolf Corp.* v. *Commissioner,* 2 T. C. 751, in which the whole Tax Court without dissent decided that the average cost rule was proper even for determining the cost of new shares exchanged for old shares in the same corporation in a recapitalization on the theory that the old shares lost their identity when traded for the new shares and that identification was not possible.

In the present case the only evidence offered for the purpose of establishing identification between the old shares and the new shares was Paragraph X of the stipulation (R. 22) relating to the matching of certificate numbers. As has been shown, even though certificate numbers were matched against each other, the matching, unless shown to rest on a factual basis of identity, would be without legal significance to identify shares. The stipulation fails, however, to show even that there was an intent to identify particular shares with particular shares through the device of matching certificates.

In the case of the preferred stock exchange the stipulation shows only that the whole block of 865 Great Western preferred shares represented by 9 certificates was surrendered all at one time and $162\frac{3}{16}$ shares of Dow common represented by three certificates were issued in lieu thereof. Not only, therefore, is evidence lacking of an intent to identify shares by matching numbers in the case of the preferred

stock exchange, but there is even no proof that a particular certificate of Dow was issued in lieu of, or matched with, any particular certificate or certificates of Great Western preferred. From this group 162 shares of Dow stock represented by two certificates were sold in 1940 (R. 22), but it is not possible to ascertain exactly against which preferred stock certificates those Dow certificates were issued. Consequently none of the Dow shares sold in 1940 have been identified with any particular Great Western preferred shares, even through the arbitrary method of matching certificates.

Nor was there identification in the case of the common stock exchange. Although the stipulation shows that two 100-share certificates in Dow were issued by the transfer agent in lieu of two 100-share certificates of Great Western, and a 50-share certificate in Dow in lieu of two Great Western certificates representing a total of 50 shares (R. 22), this particular alignment of certificates was manifestly due, not to design, but to the fact that the same numbers of shares were being exchanged. The issuance of new certificates in 100-share denominations in lieu of the old shares in that denomination conformed to custom and convenience and was not the result of any intent, so far as the stipulation shows, to identify certain shares with certain shares through matching certificates. Thus the matching of certificates is without significance for identification purposes. But even if it could be construed as an effort by the transfer agent actually to identify the shares by certificate numbers,

the stipulation fails to show what criteria guided it. Since every share of Dow was like every other share, it is apparent that the only criteria the agent could have used would have been purely arbitrary. We submit that the mere alignment of certain certificates, without some evidence, first, of an intent to identify shares through matching certificate numbers, and second, of real identification between the shares resting on some factual basis, is not sufficient to identiy any new share with any old share.[9]

But even if it be assumed *arguendo* that the arbitrary matching of certificates in the case of the exchange of Great Western common stock for Dow stock was sufficient identification, only 50 of the 212 shares sold in 1940 were received in 1939 in lieu of old common stock. The remaining 162 shares sold in 1940 have not been identified with particular old preferred shares. Thus, although the cost to taxpayer of the 50 shares may be determinable, assuming there was identification, by reference to the cost of the old common shares with which they were identified, the

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[9] The Tax Court stated (R. 47)—

The shares of Dow sold by the petitioners in 1940 are traceable through stock certificate numbers to specific shares of Great Western which were turned in in exchange

We do not construe this as a finding that there was identification in a legal sense of the old shares with the new, but if it should be interpreted as a finding that there was identification, we dispute its accuracy. The only evidence before the Tax Court relating to identification was Paragraphs X and XI of the stipulation (R. 22) and the Tax Court's statement must necessarily be based upon those paragraphs. The inferences to be drawn from the stipulation have been discussed above and they do not sustain the Tax Court's statement.

cost of the 162 shares can not be determined by reference to any particular old preferred shares. The basis for the 162 shares must therefore be determined in any event by averaging the cost of all old preferred shares over the Dow shares received in lieu thereof. And we submit that in the absence of complete identification of all the shares, the average cost method should be used to determine the basis of all the stock acquired in one exchange, rather than a hybrid system of one method for part of the stock and another method for the balance.[10]

It could not be fairly asserted in this case that identification has been made on the basis of showing identity or similarity of the old and new shares. There is unequivocal evidence that the shares in the new company were not the same as the old shares. The new share represents a proportional interest in a different corporation with different assets than did the old share. The old Great Western common and preferred shares represented an interest in a California corporation which manufactured products from salt and soda concentrates by electro-chemical processes. (R. 21.) The shares of Dow represented interests in a corporate enterprise which produced

[10] The Tax Court stated (R. 47) that the cost to taxpayer of the Great Western shares represented by the 212 shares of Dow stock sold by her was $13,900.17. This figure is not contained in the stipulation and can only have been computed by the hybrid system indicated above, of using actual cost for the Great Western common shares represented by 50 Dow shares, and computing the cost of 162 of the shares sold by averaging the cost of all the Great Western preferred shares over all the Dow shares received in lieu thereof.

heavy, intermediate, industrial, pharmaceutical, and aromatic chemicals, solvents, dyes, insecticides, metals, and alloys, and also continued the business formerly carried on by Great Western. (R. 21.) Consequently the proportionate interest in the corporate assets represented by a particular share of Great Western stock, either common or preferred, was not identical or even related, so far as the record shows, with the interest represented by a Dow share after the merger, nor was the value of the old and new shares shown to be identical or even approximately the same. Cf. *Helvering* v. *Stifel, supra.* In view of these facts, there is no merit to the taxpayer's contention (Br. 21) that identity existed between the old and new shares because the identity of the old corporation somehow persisted or continued in the new corporation. Even if it could be said that the old corporation continued, which we dispute, its shares ceased to exist and were not replaced by new shares which were identical or similar.

Taxpayer contends (Br. 15–17) that each new share has been identified with a corresponding old share by operation of law by reason of the fact that on the date of the merger each share of Great Western was separately exchanged for a Dow share or fraction thereof. It has already been shown that the exchange was not share for share but that taxpayer's entire stock interest in the old corporation was exchanged for an interest in the new in one transaction. But even if it be assumed *arguendo* that the taxpayer correctly contends that the exchange was

completed by operation of law on a share for share basis on the date the merger became effective, there has been no identification of particular old shares with any of the new shares sold in 1940. It can be said under this theory that each old share was exchanged for a new share or fraction thereof, but it is impossible to say which old share was exchanged for which new share. By disregarding the exchange of certificates in 1939 and relying only on the intangible exchange of stock interests which took place upon the merger, the taxpayer has also eliminated the one possible means available to her upon this record, that is, the matching up of stock certificates, for identifying the shares sold in 1940 as having been exchanged for any particular block or blocks of old stock. Consequently, under taxpayer's own theory it is impossible to determine the cost basis of any new share sold by identifying that share with a particular old share, and she is relegated to the average method of determining cost of the shares sold in 1940.

Taxpayer also argues (Br. 19–22) that identity of the old stock with the new is established in her case by operation of law equally as in the *Kraus* and *Fuller* cases. Those cases involved the problem of identifying old and new shares in the same corporation, whereas the instant case presents the problem of identifying the shares of one corporation with those of another. Assuming that this difference is immaterial, however, the test of identity prescribed in those cases was identification of a specific old share or shares with a specific new share or shares by

means of evidence, and in neither case was it held that identity was established by operation of law. The instant case fails to meet that test; here there was no identification of specific shares by any method.

CONCLUSION

The decision of the Tax Court should be affirmed.
Respectfully submitted.

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No. 10,697

United States Circuit Court of Appeals

For the Ninth Circuit

AMELIA DAVIS BLOCH,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Upon Petition to Review a Decision of the Tax Court of the United States

PETITIONER'S REPLY BRIEF

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No. 10,697

United States Circuit Court of Appeals

For the Ninth Circuit

AMELIA DAVIS BLOCH,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Upon Petition to Review a Decision of the Tax Court of the United States

PETITIONER'S REPLY BRIEF

I.

RE STATEMENT OF QUESTION INVOLVED

Petitioner in March, 1940 sold 212 common shares of The Dow Chemical Company (hereinafter called Dow) which she had acquired in exchange for preferred and common shares of Great Western Electro-Chemical Company (hereinafter called Great Western) in connection with the statutory merger of Great Western with and into Dow. Petitioner contends that the basis of such Dow shares is to be determined by reference to the specific Great Western shares for which they were exchanged. Respondent contends that the basis of the Dow shares sold is

to be determined by dividing the aggregate cost of all Great Western shares held by Petitioner immediately prior to the effective date of the statutory merger by the number of Dow shares acquired by her on the statutory merger and multiplying the result that is obtained by 212, the number of shares sold. (For convenience this method shall be referred to by the name given to it by Respondent, viz: the "average cost rule" [Resp's. Br. p. 10].)

It is conceded by both parties that the statutory merger was a "reorganization" under Section 112(g)(1), the exchange of the Great Western shares for Dow shares is "tax free" under Section 112(b)(3), and the basis of the Dow shares acquired on the statutory merger—and, consequently, the determination of the question here presented—is governed by the provisions of Section 113(a)(6) (Op. Br. pp. 9-11; Resp's. Br. pp. 9-16).

It is established by the decisions and admitted by Respondent (Resp's. Br. pp. 15, 27) that under Section 113(a)(6) the basis of shares of a corporation acquired in a "reorganization" in exchange for shares of the same corporation is the same as the basis of the specific shares for which they were exchanged.

> *Fuller v. Commissioner* (C.C.A. 1st, 1936) 81 Fed.(2d) 176.
>
> See, also, *Kraus v. Commissioner* (C.C.A. 2d, 1937) 88 Fed.(2d) 616.

Respondent seeks to distinguish the rule of the *Fuller* and *Kraus* cases on the ground that the instant case involved the exchange of stock of *one* corporation for stock of *another* corporation and, in support of this distinction, relies upon the decision of the United States Board of Tax Appeals in *Fleischmann v. Commissioner* (40 B.T.A. 672).*

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*Respondent also cites the decision of the Third Circuit Court of Appeals in *Arrott v. Commissioner* (C.C.A. 3d, 1943) 136 Fed.(2d) 449. However, the language quoted is dictum, since no identification between the shares acquired and the shares surrendered was established. This point is conceded by Respondent (Resp's. Br. p. 19).

Petitioner in her Opening Brief relied on two alternative grounds.

First: The instant case is governed by the rule of the *Fuller* and *Kraus* cases and not by the rule of the *Fleischmann* case. In the *Fleischmann* case—which involved the basis of stock of the transferee corporation acquired in exchange for stock of the transferor corporation on a reorganization involving a transfer of assets by the transferor to the transferee—there was no identity between the shares of the transferor corporation and the shares of the transferee corporation, nor between the transferor corporation and the transferee corporation. In the instant case —which involves a statutory merger—such identity between the Great Western and Dow shares and between Great Western and Dow is established by law (Op. Br. pp. 11-24).

Second: The rule of the *Fleischmann* case is wrong; there being no justification under Section 113(a)(6) for a distinction —sanctioned by the *Fleischmann* case—in the manner of determination of the basis of stock of a corporation acquired on a "reorganization" depending on whether received in exchange for (i) stock of the same corporation, or (ii) stock of another corporation (Op. Br. pp. 25-28).

Petitioner in this brief will first discuss Respondent's argument on the First ground and then Respondent's argument on the Second ground.

II.

RESPONDENT IS MISTAKEN IN HIS CONTENTION THAT A STATUTORY MERGER IS NOT DISTINGUISHABLE IN LEGAL EFFECT FROM A REORGANIZATION INVOLVING A TRANSFER BY ONE CORPORATION OF ITS ASSETS TO ANOTHER CORPORATION AND THE ISSUANCE BY THE TRANSFEROR CORPORATION OF ITS STOCK IN EXCHANGE FOR THE STOCK OF THE TRANSFEREE CORPORATION.

Respondent takes the position that an exchange of stock on a statutory merger is not distinguishable from an exchange of stock of a transferor corporation for stock of a transferee corporation in connection with a "reorganization" in which the transferee transfers its assets to the transferor and, in support of his position, argues:

(a) The Great Western shares were not individually exchanged for Dow shares, either by (i) operation of law, or (ii) the Merger Agreement (Resp's. Br. pp. 16-17 and footnote 7).

(b) The Federal Courts in applying the Federal Tax statute should disregard any provision of local law providing for such individual exchange in order "to give the statute uniform application" (Resp's. Br. p. 16, footnote 7).

(c) The first exchange and the second exchange referred to in Petitioner's Opening Brief (Op. Br. pp. 11-13) are one integral transaction which was not consummated until the issuance of the Dow certificates. The Great Western certificates, from and after the effective date of the merger, did not represent any interest in Dow (Resp's. Br. p. 17, footnote 8).

(d) There is no identity between the Great Western shares and the Dow shares, since the respective interests represented thereby are different. It is impossible to identify any individual Great Western share with the Dow share into which it is converted (Resp's. Br. pp. 25-27).*

---

*Respondent also at some length (Resp's. Br. p. 14) discusses an argument, imputed to Petitioner, that, since the instant exchange was an involuntary exchange, the rule of the *Arrott* case, *supra,* is not appli-

Respondent does not take issue with Petitioner's petition under Point V-D of her Opening Brief (Op. Br. pp. 23-24) that there was identification between the certificates on the certificate exchange (e. g., the second exchange) assuming that at the time of the certificate exchange the Great Western certificates represented Dow shares. Respondent's argument under point 2 (Resp's. Br. pp. 18-26) in respect of the certificate exchange appears to be predicated on the assumption that the Great Western certificates did not represent Dow shares at the time of the certificate exchange and on such certificate exchange certificates representing shares in one corporation (apparently, Great Western) were exchanged for certificates representing shares in another corporation (i. e., Dow).

It is respectfully submitted that none of Respondent's arguments can be supported and that accordingly his entire position on this head must fail.

(a) The Great Western shares were individually exchanged for Dow shares by operation of law and the Agreement of Merger.

Both Section 52 of the Michigan General Corporation Act and Section 361 of the California Civil Code direct that the Agreement of Merger shall provide the "manner of *converting* the shares of each of the constituent corporations into shares of the consolidated or merged corporation" (italics supplied).*

Article III of the Agreement of Merger, pursuant to said statutory direction, provides that on the effective date of the merger, each common share of Great Western shall be consti-

*In California Civil Code Section 361 the words "and basis" are added after the word "manner"; the words "each of" are omitted and the word "surviving" is substituted for the word "merged".

cable. Petitioner argued in her Opening Brief that the instant exchange was effected by operation of law but did not claim it was involuntary (Op. Br. pp. 15-22). There is a clear distinction between an exchange by operation of law and an involuntary exchange (*U. S. v. Seattle-First National Bank* (1944) 321 U.S. 583). Accordingly, Respondent's argument in respect of this claimed position of Petitioner is irrelevant.

tuted and converted into one common share of Dow and each preferred share of Great Western shall be constituted and converted into 3/16ths of one common share of Dow. Sections 52 and 53 of the Michigan General Corporation Act and Section 361 of the California Civil Code provide that the Agreement of Merger shall become effective upon the compliance with the statutory requirements of filings, etc. Accordingly, on the effective date of the Agreement of Merger, the Great Western shares were *converted* into Dow shares, as provided in the Agreement of Merger.

U. S. v. Seattle-First National Bank, 321 U.S. 583;
National Supply Co. v. Leland Stanford Jr. University (C.C.A. 9th Circuit, 1943) 134 Fed.(2d) 689;
Copeland v. Minong Mining Co. (1875) 33 Mich. 2;
Ridgway v. Griswold (1878) 20 Fed. Cas. C.C.D. Kansas, Case No. 11819.

See, also, Opening Brief pages 15-20.

Respondent argues that under the statutory provisions above referred to, the individual shares of Great Western were not exchanged for individual shares of Dow and that the provision of Article III of the Statutory Merger, despite its explicit language to the contrary, provides merely for a *rate* of exchange and does not provide that each individual share of the Great Western stock shall be separately converted into or exchanged for a Dow share or fractional Dow share (Resp's. Br. p. 16, footnote 7, p. 17).

This contention is directly contrary to the entire concept of merger law, it being established that on a merger the corporate identity of the merging corporation is merged into that of the surviving corporation and the stock interests in the merging corporation are converted into stock interests in the surviving corporation.

U. S. v. Seattle-First National Bank, supra;
National Supply Co. v. Leland Stanford Jr. University, supra;

Copeland v. Minong Mining Co., supra;
Ridgway v. Griswold, supra.

No word more apt than the word actually used in the statutes and in the Merger Agreement, viz: "convert", could have been used to convey the intention that the individual share-interest or shares in the merging corporation should be changed into individual share-interests or shares of the surviving corporation. Accordingly, since each individual share of the Great Western was converted into a share or fractional share of Dow on the effective date of the statutory merger, it follows that, in effect, such share of Great Western was "exchanged" on such date for the share or fractional share of Dow into which it was converted.

(b) The Federal Courts in applying the Tax Statutes should give effect to the provisions of the merger statutes.

Respondent argues that the instant exchange "is factually essentially the same as other reorganization exchanges *occurring in other states* and must receive the same treatment under the Federal basic statute in order to give the statute uniform application" (italics supplied) (Resp's. Br. p. 16, footnote 7). The implication of this argument is that the merger statutes in question are peculiar to the laws of Michigan and California. Quite the contrary is true, since most states have merger statutes which are substantially identical. Thirty-nine out of the forty-eight states have general merger statutes, and two more have merger statutes applicable only to certain limited classes of corporations. Only seven states have no merger statute at all.

The distinction is not between a statutory merger occurring in *Michigan or California* and a merger occurring in other states, but between a statutory merger, on the one hand, and a reorganization involving a simple transfer of assets from one corporation to another corporation, on the other hand. The United

States Supreme Court in two cases has recognized and given effect to this distinction.

U. S. v. Seattle-First National Bank, supra;
Helvering v. Metropolitan Edison Co. (1939) 306 U.S. 522.
See, also, *National Supply Co. v. Leland Stanford Jr. University, supra.*

For a discussion of the above cases see Opening Brief p. 21.

(c) **The first exchange and second exchange referred to in the Opening Brief are separate transactions. The Great Western certificates from and after the effective date of the merger represented stock interests in Dow.**

Respondent argues (Resp's. Br. p. 17, footnote 8) that the first exchange and second exchange (Op. Br. pp. 11-13) must be regarded as one transaction which was consummated upon the certificate exchange in 1939, and in support of his argument cites cases holding that on a "reorganization" the various integral steps must be regarded as part of one transaction. This argument cannot be sustained. The "plan of reorganization" in the instant case was the statutory merger of Great Western with and into Dow. This took place on or before December 31, 1938. The subsequent 1939 certificate exchange, which took place several weeks later (Record p. 72), was not a part of, and had nothing to do with the statutory merger (see Op. Br. pp. 11-13).

Respondent argues that, while the Great Western stockholders on the effective date of the merger may have acquired an interest in Dow assets, the Great Western certificates did not represent such interest. Clearly this interest was a stock interest, since we have shown the Great Western shares were converted into Dow shares on the effective date of the merger. Since the Great Western certificates immediately prior to the effective date of the merger represented Great Western shares, and on such date the

Great Western shares were converted into Dow shares, it follows that the Great Western certificates thereafter represented such Dow shares.

(d) The identity between the Great Western shares and Dow shares is established by operation of law. The identity between the shares represented by each Great Western certificate after the effective date of the merger and the Great Western share represented thereby immediately prior to such date is clearly established.

Respondent argues that since the business interest represented by the Great Western shares is entirely different from the business interest represented by the Dow shares that the Great Western shares may not be identified with the Dow shares (Resp's. Br. pp. 25-26). The complete answer to Respondent's contention is that such identification is provided by the applicable provisions of the laws of the states of Michigan and California (Secs. 52 and 53 of the Michigan General Corporation Laws and Sec. 361 of the California Civil Code) and the Federal Courts, in applying the Federal Tax statutes, will give effect to such statutory provisions (see supra, pp. 7-8). The situation presented is no different in a case where a corporation acquires an entirely new business. In such case the identity of the shares of the corporation is unaffected. (*Rhode Island Hospital Trust Company v. Doughton* (1926) 270 U.S. 69.)

Respondent further argues that on Petitioner's theory no identity can be established between the individual Great Western shares and the Dow shares for which they were exchanged (Resp's. Br. pp. 26-27). This is not so. There is complete identity established between the Dow shares represented by each Great Western certificate after the effective date of the merger and the Great Western shares represented thereby immediately prior to said date (Op. Br. pp. 16-17).*

*Respondent in other parts of his brief does not appear to have any difficulty in tracing the identification (Resp's. Br. pp. 22-24).

Under this point II we have disposed of every argument of Respondent pertaining to Petitioner's first ground. Accordingly, on this basis alone the decision must be for Petitioner. We will now discuss the arguments urged by Respondent in connection with the second ground.

III.

RESPONDENT'S ATTEMPTED DISTINCTION IN THE MANNER OF THE DETERMINATION, UNDER SECTION 113(a)(6), OF THE BASIS OF STOCK ACQUIRED ON A REORGANIZATION, DEPENDING ON WHETHER THE STOCK WAS ACQUIRED IN EXCHANGE FOR (i) STOCK OF THE SAME CORPORATION, OR (ii) STOCK OF ANOTHER CORPORATION, IS WITHOUT FOUNDATION.

Respondent concedes that under Section 113(a)(6) the basis of stock of one corporation exchanged on a "reorganization" for stock of the same corporation is the same as the basis of the stock for which it is exchanged (Resp's. Br. p. 15). See *Fuller v. Commissioners, supra,* and *Kraus v. Commissioner, supra.*

Respondent argues that the rule of the *Fuller* and *Kraus* cases is not applicable to the instant case since those cases involve exchanges of stock in the same corporation and the instant case involves exchange of stock in one corporation for stock in another corporation, and that, accordingly, the average cost rule is applicable to the instant case and, in support thereof, relies upon the following grounds:

> (a) The average cost rule conforms with the reality of the situation since the Dow shares were acquired at one time and each Dow share acquired had the same value irrespective of the cost of the Great Western shares for which it was exchanged (Resp's. Br. pp. 13-14).
>
> (b) The language of Section 113(a)(6) merely requires that the basis of all the shares received on the exchange shall be the same as the basis of all the shares surrendered on the exchange (Resp's. Br. pp. 17-18).

(c) Petitioner has failed to establish any identity between the certificates surrendered and the certificates received since she has failed to prove an intention to identify (Resp's. Br. pp. 18-24).

The difficulty with Respondent's position is that (i) each of the grounds advanced is applicable equally to the "reorganization" involved in the *Fuller* and *Kraus* cases, i. e., an exchange of stock in the same corporation, and (ii) his arguments fail to give effect to the intended result of the reorganization basis provisions. It is the intention of the reorganization basis provisions that, for the purpose of determining basis of the stock acquired on the reorganization, the acquired stock should "be considered as taking the place of the old property given up in connection with the exchange" (Gregg Statement explaining Sec. 204 of the 1924 Revenue Act).*

A more detailed consideration of each of the grounds advanced by Respondent will show that none of them can be sustained.

(a) The fact that Dow shares were acquired at one time, and are of equal value to one another, is immaterial in connection with the application of Sec. 113(a)(6) and do not support the application of the average cost rule.

Respondent argues that, in view of the fact that the Dow shares were acquired on the statutory merger in exchange for Great Western shares at the same time and are of equal value, that, even though there is identification between the Great Western shares surrendered and the Dow shares acquired, it is proper to apply the average cost rule in determining the basis of the Dow shares acquired, since it conforms to realities of the situation (Resp's. Br. pp. 13-14).

The question here involved is one of statutory construction, viz: the interpretation of the provisions of Section 113(a)(6).

*In connection with the revision of the reorganization provisions by the Revenue Act of 1924, a statement (referred to as the "Gregg Statement") explaining such changes was prepared by Mr. A. W. Gregg, special assistant to the Secretary of the Treasury.

Respondent has failed to show how these factors are relevant in the construction of said section. As a matter of fact, as we shall see, infra, p. 12 to p. 15, these factors are irrelevant in view of the Congressional policy adopted in Section 113(a)(6).

Each of the factors cited by Respondent is applicable to stock of a corporation acquired on a "reorganization" for stock of the same corporation. In such case, the new stock acquired would be acquired at the same time and would have an equal value. Clearly, therefore, these factors do not distinguish the instant case from the *Fuller* and *Kraus* cases involving exchanges, on a reorganization, of stock in the same corporation in which identification is permitted.

(b) Sec. 113(a)(6) directs that, for the purpose of determining basis, the property acquired on a tax-free exchange shall be identified with the specific property for which it was exchanged.

Section 113(a)(6) provides that the basis of the property acquired "shall be the same as in the case of the property exchanged". Respondent argues that the provisions of Section 113(a)(6) "are served when the basis of all the new stock is assigned the basis of all the old stock" (Resp's. Br. pp. 17-18). However, if Section 113(a)(6), as admitted by Respondent, permits identification in the case of stock of one corporation acquired on a reorganization in exchange for stock of the same corporation why does it not likewise permit such identification in the case of stock of one corporation acquired on a "reorganization" for stock of another corporation?

The meaning attributed by Respondent to Section 113(a)(6) cannot be sustained in view of the history and language of the provision and the Congressional policy evidenced thereby. On the contrary, such history, language and Congressional policy indicate that identification for the purposes of determining basis, rather than being prohibited, is directed.

Section 113(a)(6) is derived from Section 202(b) of the Revenue Act of 1918. Section 202(b) provided that "the new stock or securities received [on a tax-free exchange] shall be treated as taking the place of the stock, securities or property exchanged" for the purposes of determining basis. A similar provision was included in Section 202(d)(1) of the Revenue Act of 1921 in a general provision relating to the basis of property acquired on tax-free exchanges.*

In the Revenue Act of 1924 there was a complete revision of the reorganization provisions and the provision in the form now contained in Section 113(a)(6) was included in Section 204(a)(6) of the Revenue Act of 1924. This provision was intended to have the same effect as Section 202(d)(1). See Report of Ways and Means Committee (68th Cong., 1st Sess., H. Rept. 179) p. 16; Report of Senate Finance Committee (68th Cong., 1st Sess., S. Rept. 389) p. 10; Gregg Statement under Section 204.

On pages 16-17 of said Report of Ways and Means Committee, in respect of said section, it is stated: "The general theory of this section is that where no gain or loss is recognized as resulting from the exchange the new property received shall, for the purposes of determining gain or loss from a subsequent sale . . ., be considered as taking the place of the old property given up in connection with the exchange. . . . These provisions are based upon the theory that the types of exchanges specified in Section 203 are merely changes in form and not in substance . . ."†

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*Section 202(d)(1) provided that "the property received shall . . . be treated as taking the place of the property exchanged therefor, . . ."

†See, also, Report of Senate Finance Committee, above cited, pages 10-12, where almost identical language is set forth. The language referred to from both the Ways and Means Committee and Senate Finance Committee Reports appears to be taken from the Gregg Statement in reference to Section 204.

Clearly the Committee Reports are relevant in construing the provisions of Section 113(a)(6) (*Helvering v. Griffiths* [1943] 318 U.S. 371). From these Reports, it is established that Congress intended by Section 113(a)(6) to provide that for the purposes of determining basis the property acquired on a tax-free exchange should be considered as taking the place of the property surrendered on the exchange. Accordingly, it is clear that Congress by Section 113(a)(6) directed that, for the purposes of determining basis, the property acquired on such exchange be identified with the property surrendered on the exchange. Furthermore, the very language of Section 113(a)(6) (viz: that the basis of the property acquired "shall be the same *as in the case* of the property exchanged" [italics supplied]) likewise directs that identification shall be made. This is no mere argument, as claimed by Respondent, that the sum of the bases of the various units of property acquired shall equal the sum of the bases of the various units of property surrendered. In view of the foregoing, it is clear that Section 113(a)(6) rather than permitting, as contended by Respondent, the application of the average cost rule, instead directs identification between the property acquired and the property exchanged for the purpose of determining the basis of the property acquired.

In view of the Congressional policy adopted in Section 113(a)(6), it is clear that the factors cited by Respondent (see supra, pp. 11-12) in supporting the application of the average cost rule (i. e., that the Dow shares were acquired at one time and have an equal value) are irrelevant since Congress has directed that the Dow shares acquired, for the purposes of determining basis, should be treated as though they were the Great Western shares exchanged.

(c) Identification between the Great Western certificates surrendered and the Dow certificates acquired has been clearly established. Identification is a matter of fact and intention is irrelevant.

Respondent argues that no identification has been established between the Great Western certificates surrendered and the Dow

certificates received, and that the finding by the Tax Court of identification between the Dow shares and Great Western shares may not be supported. He states that any such identification is entirely arbitrary, and further argues that no intention to identify the Great Western certificates surrendered with the Dow certificates received has been established excepting the act of the Transfer Agent (Resp's. Br. pp. 18-22, p. 24, footnote 9). It is respectfully submitted that the facts as stipulated support the Tax Court's finding of identification (Record p. 22).

In support of this argument, Respondent refers to the case of *Crespi v. Commissioner* (C.C.A. 5th, 1942) 126 Fed.2nd 699. In this case the charter of a corporation expired by operation of law and its assets passed to its officers and directors as trustees for the stockholders. The property was transferred to a new corporation which issued shares to taxpayer representing his interest in the property. Taxpayer endeavored to treat the transaction as an exchange of stock of the old corporation for stock in the new corporation. The court held (126 Fed.2nd 699, 701) "each share represented an aliquot part of this value [the value of the property transferred], and therefore each took the same basis as every other share." The *Crespi* case, therefore, involved an exchange of property for stock and not an exchange of stock for stock and its holding is entirely immaterial to the instant case.

Respondent argues at length, without the citation of any authority whatsoever, that identification is a matter of intention. On the contrary, it is well established by the decisions that identification is a matter of fact and intention has no relevance whatsoever in establishing identification. In the instant case it is clear from the stipulation that certain identifiable Dow certificates were issued in lieu of certain identifiable Great Western certificates (Record p. 22). Identification, therefore, as a matter of fact, between the Dow certificates acquired and the Great Western certificates surrendered, has been established. It is immaterial whether Petitioner had any foreknowledge of the specific

Dow certificates which were to be issued in lieu of the specific Great Western certificates. If, for example, a taxpayer sells certain identifiable shares but intended and directed that other shares be sold, nevertheless, for the purpose of determining gain or loss on the sale, the basis of the property sold is taken to be the basis of the property *actually sold* and not that of the property *intended* to be sold.

> *Davidson v. Commissioner* (1938) 305 U.S. 44;
> *Smith v. Higgins* (C.C.A. 2nd, 1939) 102 Fed.2nd 456;
> *Commissioner v. Merchants & Manufacturers Fire Insurance Company* (C.C.A. 3rd, 1934) 72 Fed.2nd 408;
> *Holmes v. Commissioner* (C.C.A. 3rd, 1943) 134 Fed. 2nd 219.

Furthermore, the identification between the Dow certificates issued and the Great Western certificates surrendered is the same as the identification which is established when a taxpayer receives from a corporation new certificates for old certificates. It is clear that identification may be established in such case (*James W. Arrott, Jr. v. Commissioner* [1936] 34 B.T.A. 133). Compare *Fuller v. Commissioner, supra,* where identification was permitted, in determining the basis of stock issued on a stock split-up, between the new split-up stock and the original stock. It follows from what has been said that the question of intention is immaterial in establishing identification where, as here, identification has been established as a matter of fact. The identification in the *Fuller* case is the same as in the instant case, i. e., through action of the stock transfer agent and Respondent's attempt (Resp's. Br. pp. 27-28) to distinguish the *Fuller* case is without merit.

Respondent argues that in the case of the Dow certificates issued for the Great Western preferred certificates complete identification has not been established (Resp's. Br. pp. 23-25). In the case of such shares, Dow certificates representing 162-3/16 common shares were issued as a unit for the Great Western cer-

tificates representing 865 preferred shares (Record p. 32). 162 shares of said 162-3/16 shares were sold in the transaction involved in the instant case. Clearly the Dow certificates representing said 162-3/16 shares have been identified with the Great Western preferred certificates.

Cf. *James W. Arrott, Jr. v. Commissioner supra;*
Bancitaly Corporation v. Commissioner (1936) 34 B.T.A. 494;
Melcher v. U. S., U. S. Court of Claims 1937, 19 Fed. Supp. 663.

Since said 162-3/16 Dow shares were issued as a unit for the Great Western preferred shares, it was necessary, since only part of the shares were sold in the involved transaction, to use some arbitrary method for determining basis of such shares such as the "first-in first-out" rule or the average cost rule. Petitioner in view of the rule of *Commissioner v. Von Guten* (C.C.A. 6, 1935) 76 Fed.(2d) 760, for the purposes of determining gain or loss on the sale on the portion of said 162-3/16 Dow shares sold in the instant transaction, applied the average cost rule by dividing the aggregate cost or other basis of the Great Western preferred shares by 162-3/16 and multiplying the result by 162, the number of shares sold.

Respondent claims that this results in the adoption of a hybrid rule and that, accordingly, the average cost rule should be used for all the Dow shares acquired (Resp's. Br. pp. 24-25). The same identical situation arises where a taxpayer, in one transaction, sells certain identifiable stock and also part of a block of stock. In such case it is well established that the basis of the identifiable stock is used and that the basis of portion of the block of stock sold is determined on the "first-in first-out" rule by reference to said block of stock.

Arrott v. Commissioner, supra;
Bancitaly Corporation v. Commissioner, supra;
Melcher v. U. S., supra;
G.C.M., 8426, IX-2, Cumulative Bulletin, p. 92.

It is submitted that each argument advanced by Petitioner in support of his contention that identification cannot be used in the instant case has been fully answered.

IV.

CONCLUSION

In view of the foregoing, it is respectfully submitted that the decision of the Tax Court should be reversed.

Respectfully submitted,

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